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News Round-up

- ▶ NTPC (NATP IN) has commissioned a second unit of 490 MW at its Dadri project. With this development, two coal-based units of 490 MW each have been commissioned at NTPC-Dadri project to meet the power requirement during the Commonwealth games. *(BSTD)*
- ▶ Sun Pharmaceuticals Industries (SUNP IN) said the US District Court for New Jersey had denied its appeal to reverse an earlier jury verdict in the patent litigation over the generic version of Wyeth's heartburn medicine, Protonix. *(BSTD)*
- ▶ ICICI Bank (ICICIB IN) said it expected lending rates to go up after September as credit offtake was likely to pick up in the second half of the current year. *(BSTD)*
- ▶ BHEL (BHEL IN) has bagged USD 0.55 mn contract from Dainik Bhaskar Power Ltd (DBPL) to build a 1,200-mw thermal power plant in Chattisgarh. *(FNLE)*
- ▶ ONGC (ONGC IN) submits viability report of 9 gas blocks to DGH. *(FNLE)*
- ▶ BSNL said it had sought a refund of the USD 3.95 bn it paid for 3G and broadband spectrum and had written a letter to the Department of Telecommunications for the same. *(BSTD)*
- ▶ Tata Steel (TATA IN) began talks with lenders, including Citigroup, to refinance as much as USD 5.4 bn in loans for its UK unit. *(ECNT)*
- ▶ L&T General insurance all set to commence operations. The co will roll out its first set of products in the next two months. *(THBL)*
- ▶ Bajaj Auto (BJAUT IN) to switch to completely knocked-down (CKD) assembling at Indonesian plant. This move will attract lower custom duties. *(THBL)*
- ▶ Adani Group pads up to make USD 300 mn acquisition pitch for DeccanChargers. *(FNLE)*
- ▶ Canara Bank (CBK IN) could possibly look at raising USD 106.38-127.66 mn through debt route over the next few weeks. *(ECNT)*

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

EQUITY MARKETS

India	Change %			
	19-Jul	1-day	1-mo	3-mo
Sensex	17,928	(0.2)	2.0	2.7
Nifty	5,386	(0.1)	2.4	3.0
Global/Regional indices				
Dow Jones	10,154	0.6	(2.8)	(8.7)
Nasdaq Composite	2,198	0.9	(4.8)	(12.1)
FTSE	5,148	(0.2)	(2.0)	(11.0)
Nikkie	9,304	(1.1)	(6.9)	(14.7)
Hang Seng	20,076	(0.1)	(1.0)	(7.2)
KOSPI	1,729	(0.2)	1.0	0.6
Value traded – India				
Cash (NSE+BSE)	145		169	170
Derivatives (NSE)	787		987	1,082
Deri. open interest	1,579		1,502	1,257

Forex/money market

	Change, basis points			
	19-Jul	1-day	1-mo	3-mo
Rs/US\$	47.1	34	137	238
10yr govt bond, %	7.6	(2)	3	(43)
Net investment (US\$m)				
	16-Jul		MTD	CYTD
Fls	162		1,771	8,471
MFs	(37)		(276)	(282)

Top movers -3mo basis

Best performers	Change, %			
	19-Jul	1-day	1-mo	3-mo
HPCL IN Equity	448.4	0.0	31.8	49.3
BJFIN IN Equity	425.4	2.3	5.3	35.8
IOCL IN Equity	377.1	(0.3)	12.8	34.1
BPCL IN Equity	655.5	(0.8)	25.6	30.8
AL IN Equity	72.7	3.0	16.1	30.3
Worst performers				
ABAN IN Equity	845.8	(1.8)	15.7	(30.3)
RNR IN Equity	44.8	(1.1)	(28.7)	(28.5)
TATA IN Equity	511.3	0.5	7.9	(23.8)
SESA IN Equity	348.4	1.5	(1.5)	(23.6)
ICEM IN Equity	108.1	0.0	(4.7)	(20.6)

JULY 19, 2010

NEW RELEASE

BSE-30: 17,928

Closing two trades, starting two more. We have closed two of our current Alpha Bet trades—(1) Long ONGC, Short Cairn with a gross return of -4.4% since inception and (2) Long LT, Short Siemens with a gross return of +11.7%. We have opened two new trades—(1) Long M&M, Short Hero Honda and (2) Long HDFC Bank, Short HUL. Exhibit 1 gives the returns of our recent Alpha Bet trades.

Closing Long ONGC, Short Cairn trade

The Long ONGC, Short Cairn has given -4.4% return since February 10, 2010 despite many of our identified triggers—(1) natural gas price increase and (2) partial deregulation of auto fuels for ONGC's absolute performance having come through. A fresh trade initiated by our US sales team has delivered +18.5% gross return since April 12, 2010. ONGC stock has moved up 15.8% from February 10, 2010 but Cairn stock has gone up 21.2% on (1) an upgrade of reserves in March 2010 and (2) the market's faith in high crude oil prices.

Closing Long LT, Short Siemens

The Long LT, Short Siemens trade has delivered +11.7% gross return since June 11, 2010. We are not sure about further absolute performance of LT stock in the short term given its +5.3% move over the past month and rich valuations (20.9X FY2012E EPS).

Keeping open (1) Long Grasim, Short ACEM and (2) Long Infosys, Short Bharti trades

We expect Grasim stock to re-rate from current levels; its current stock price is factoring 32% holding-company discount for its 60% investment in UltraTech Cement (comprising all of Grasim's cement business) post the ongoing restructuring exercise. We are also keeping open our Long Infosys, Short Bharti trade despite Infosys' weak 1QFY11 results. We find the recent euphoria surrounding Indian telecom sectors completely misplaced given (1) continued subtle pricing competition as opposed to visible headline price reduction earlier, (2) likely large value destruction from high 3G and BWA license fees and (3) potential negative regulatory risks.

Opening new trades—(3) Long M&M, Short Hero Honda and (4) Long HDFC Bank, Short HUL

We open two new trades—(3) Long M&M, Short Hero Honda and (4) Long HDFC Bank, Short HUL to derive advantage from the likely positive performance of our long trades and likely decline in absolute prices of our short trades due to competitive issues in their sectors. Both our short stocks are trading at near-peak multiples but the companies are losing market share to more aggressive competitors or new entrants.

QUICK NUMBERS

- Performance of recent Alpha Bet trades
- Long M&M, Short HH
- Long HDFC Bank, Short HUL

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KIE Alpha Bet trades

Statistics of trades, current price, initiation price, gross expected/actual return

	Stock	Current price (Rs)	Initiation price (Rs)	Return (%)
Trade 1 (Started June 11, 2010)				
Buy	Infosys Technologies	2,770	2,631	5.3
Sell	Bharti Airtel	298	274	8.6
	Starting ratio (X)	9.3	9.6	(3.0)
Current return (%) (3.0)				
Trade 2 (Started June 11, 2010)				
Buy	Grasim Industries	1,828	1,820	0.5
Sell	Ambuja Cements	108	115	(6.2)
	Starting ratio (X)	17.0	15.8	7.1
Current return (%) 7.1				
Trade 3				
Buy	Mahindra & Mahindra		606	
Sell	Hero Honda		1,957	
	Starting ratio (X)		0.3	
Target return (%) 10.0				
Trade 4				
Buy	HDFC Bank		2,048	
Sell	Hindustan Unilever		265	
	Starting ratio (X)		7.7	
Target return (%) 10.0				
Closed trade (Feb 10, 2010 - July 19, 2010)				
Buy	Oil & Natural Gas Corp.	1,259	1,087	15.8
Sell	Cairn India	315	260	21.2
	Starting ratio (X)	4.0	4.2	(4.4)
Return (%) (4.4)				
Closed trade (Feb 10, 2010 - July 19, 2010)				
Buy	Larsen & Toubro	1,894	1,677	13.0
Sell	Siemens	726	718	1.2
	Starting ratio (X)	2.6	2.3	11.7
Return (%) 11.7				
Closed trade (Feb 10, 2010 - Jun 11, 2010)				
Buy	Tata Steel	474	522	(9)
Sell	Hindalco	140	137	2
	Starting ratio (X)	3.4	3.8	(11.2)
Return (%) (11.2)				
Closed trade (April 27, 2010 - Jun 11, 2010)				
Buy	HDFC Bank	1,946	1,980	(2)
Sell	ICICI Bank	846	947	(11)
	Starting ratio (X)	2.3	2.1	10.0
Return (%) 10.0				
Closed trade (April 27, 2010 - Jun 11, 2010)				
Buy	Mahindra & Mahindra	607	537	13
Sell	Maruti Suzuki	1,357	1,283	6
	Starting ratio (X)	0.4	0.4	6.9
Return (%) 6.9				
Closed trade (Feb 10, 2010 - Apr 27, 2010)				
Buy	HDFC Bank	1,980	1,594	24
Sell	Axis Bank	1,277	1,025	25
	Starting ratio (X)	1.6	1.6	(0.3)
Return (%) (0.3)				
Closed trade (Feb 10, 2010 - Apr 22, 2010)				
Buy	Jaiprakash Associates	153	128	19
Sell	ACC	920	870	6
	Starting ratio (X)	0.2	0.1	12.4
Return (%) 12.4				

Source: Kotak Institutional Equities estimates

JULY 19, 2010
RESULT

 Coverage view: **Attractive**

 Price (Rs): **2,048**

 Target price (Rs): **2,400**

 BSE-30: **17,928**

Impressive as ever. HDFC Bank 1Q earnings remained on track, with key highlights being: (1) Faster loan growth of 41% yoy, (2) margins declined by only 10 bps qoq to 4.3% despite savings deposit impact, and (3) gross NPLs declined further; provisioning coverage at 78%. We believe that HDFC Bank has reasonable buffers to sustain its growth and earnings momentum over next two years at least. It remains our preferred pick amongst private banks despite expensive valuations of 3.3XFY12E PBR. **BUY.**

Company data and valuation summary

HDFC Bank

Stock data

52-week range (Rs) (high,low)	2,111-1,353
Market Cap. (Rs bn)	937.4

Shareholding pattern (%)

Promoters	23.7
FIs	44.3
MFs	4.4

Price performance (%)

	1M	3M	12M
Absolute	2.8	5.9	42.5
Rel. to BSE-30	0.8	2.8	17.2

Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	64.4	87.2	113.8
EPS growth (%)	22.1	35.4	30.5
P/E (X)	31.8	23.5	18.0
NII (Rs bn)	83.9	100.7	121.5
Net profits (Rs bn)	29.5	39.9	52.1
BVPS	470.2	538.4	627.4
P/B (X)	4.4	3.8	3.3
ROE (%)	16.1	17.3	19.5
Div. Yield (%)	0.6	0.8	1.0

In-line performance for the quarter; outlook remains strong

HDFC Bank maintained its trend of quality performance across most parameters (1) loan growth, even after adjusting for short-term lending, continues to remain impressive at a pace that is well ahead of industry. Retail is showing traction aided by housing and vehicles. The bank is participating opportunistically on corporate loans without diluting margins, (2) margins are healthy at 4.3% despite the savings rate impact, but we expect a marginal decline going forward as the proportion of corporate increases and the impact of higher equity wears off, and (3) the pace of new NPL formation has peaked and new delinquencies are much lower than the previous few quarters - likely to result in lower absolute NPLs and credit provisioning.

The strong core operational performance has helped negate losses on its treasury book and maintain earnings momentum. We believe HDFC Bank has enough cushions on costs and provisions to maintain its impeccable earnings momentum. We have maintained our earnings but revised our TP to Rs2,400 (from Rs2,200 earlier), rolling our financials to FY2012E.

Loans growth impressive at 41% yoy; opportunistic on telecom

HDFC Bank's loan book grew by 16% qoq (normalized qoq growth is about 8-9%) and 41% yoy to Rs1.46 tn as of June 2010, mainly due to higher growth in corporate loans (mainly in telecom). Corporate loans grew by 65% yoy (30% qoq) while retail grew by 24% yoy (5% qoq), now about 52% of loan book. Retail loans were largely driven by auto loans (up 33% yoy at Rs214 bn), commercial vehicles (up 30% yoy at Rs100 bn) and mortgages (53% yoy at Rs95 bn, largely bought from HDFC - Rs9 bn during the quarter).

QUICK NUMBERS

- **Loan growth at 41% yoy while NII growth at 29% yoy**
- **Pressure on fee income continues (15% yoy growth)**
- **Maintained earnings. Raising TP to Rs2,400 (from Rs2,200)**

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CASA ratio declines 280 bps to 49% as growth takes precedence

Despite a healthy CASA deposits growth of 37% yoy (3% qoq), CASA ratio declined qoq by 280 bps to 49% as (1) growth took precedence funded by term deposits, and (2) seasonal trend in 1QFY10. Savings deposits grew by 40% yoy and current deposits grew by 34% yoy. With likely strong loan growth and higher interest rates, CASA growth was expected to decline in FY2011E, but it still remains a structural advantage for the bank. Deposits growth remained well ahead of industry at 26% yoy and 9% qoq.

Margins decline 10 bps qoq but CD ratio cushions decline

NIMs for the quarter were at 4.3% (sequential decline of 10 bps) as the bank relied on term deposits to fund growth coupled with the impact of revised savings deposit interest. Sharp improvement in CD ratio to 79% from 75% in March 2010 cushioned the NIM decline. NII grew by 29% yoy in 1QFY11, in line with our estimates. Our calculation suggests that funding costs had increased by 40 bps qoq but declined by 150 bps from 1QFY10.

We expect margins to moderate further as the bank would need to raise deposit rates sooner as the outlook on credit remains strong and the bank has little cushion on its investment book. The bank strives to maintain margins at 4-4.2%. We expect margins to decline by 10 bps in FY2011E.

Asset quality trend healthy; coverage ratio healthy at 77%

Gross NPLs declined, fourth quarter in succession, by about 17% yoy (1% qoq) in 1QFY11 to Rs17.9 bn. New NPL formation continues to reduce over the past few quarters. Despite lower NPL formation, loan loss provisioning for the quarter was higher at 120 bps compared to a lower LLP of 90 bps in March 2010. We are building in provisions of 120 bps for HDFC Bank in FY2011E and FY2012E. We believe that the slippages (net of recoveries) were about Rs3.5 bn, about 1.2% of loans.

The bank continues to make higher provisions and write-offs (compared to regulatory norms) resulting in much lower net NPLs at 0.3%. However, the bank has changed its policy on floating provisions (Rs650 mn) taking to tier-2 capital instead of netting off against gross NPLs as provision coverage ratio remains healthy at 77%. The total restructured continued to be low at 0.3% of loans.

Fee income growth slower at 15% yoy

Non-interest income declined by 10% yoy to Rs9.4 bn, as treasury gains was just Rs215 mn, against a gain of Rs2.6 bn in 1QFY10. Core fees growth was slower at 15% yoy in 1Q to Rs7.5 bn as pricing pressure remains on retail fees, especially third party products. Also, lower credit card fees and revised fee charges impacted overall fee income growth. Exchange income increased by 25% yoy. We are factoring 18% CAGR for FY2010-12E.

Others key highlights

- ▶ Other provisions include provisions for MTM against foreign currency derivatives (client related) and provisions for receivables on account of properties, related to CBOP – we believe that the bank is very conservative on this count, and these provisions could get reversed in future quarters.
- ▶ Operating costs have increased by 15% yoy mainly due to sharp increase in staff expenses (19% yoy).
- ▶ Overall branches for the quarter have remained flat for two quarters in succession at 1,725 branches. Cost-income ratio was flat sequentially at 48%.

HDFC Bank, quarterly performance

March fiscal year-ends, 1QFY10-1QFY11 (Rs mn)

	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11	% chg	1QFY11	Actual Vs KS
Interest income	40,931	39,919	40,348	40,531	44,202	8.0	42,648	3.6
Interest on advances	30,178	30,102	30,389	30,314	33,105	9.7	31,396	5.4
Interest on investments	10,334	9,596	9,802	10,081	10,532	1.9	11,115	(5.2)
Other interest	419	221	157	136	564	34.6	136	314.5
Interest expense	22,375	20,361	18,109	17,018	20,190	(9.8)	18,679	8.1
Net interest income	18,556	19,558	22,239	23,514	24,011	29.4	23,969	0.2
Non-int.income	10,437	10,074	8,530	9,036	9,399	(9.9)	9,683	(2.9)
- fee income	6,493	6,924	7,237	7,653	7,457	14.8	7,792	(4.3)
- exchange income	1,378	1,510	1,540	1,801	1,718	24.7	1,791	(4.1)
- sale of invts.	2,560	1,629	(265)	(473)	215	(91.6)	100	115.0
Non treasury income	7,877	8,445	8,795	9,509	9,184	16.6	9,583	(4.2)
Total income	28,992	29,632	30,769	32,549	33,410	15.2	33,652	(0.7)
Op. expenses	13,806	13,702	14,532	15,605	15,923	15.3	17,257	(7.7)
Employee cost	5,593	5,541	5,786	5,972	6,671	19.3	6,992	(4.6)
Other cost	8,212	8,161	8,746	9,634	9,252	12.7	10,266	(9.9)
Operating profit	15,187	15,930	16,237	16,944	17,487	15.1	16,394	6.7
Provisions and cont.	6,588	5,941	4,477	4,399	5,550	(15.8)	4,262	30.2
NPLs	6,310	5,941	4,379	2,750	3,650	(42.2)	2,613	39.7
PBT	8,598	9,989	11,760	12,545	11,937	38.8	12,133	(1.6)
Tax	2,537	3,114	3,575	4,178	3,820	50.6	4,041	(5.5)
Net profit	6,061	6,875	8,185	8,366	8,117	33.9	8,092	0.3
Tax rate (%)	29.5	31.2	30.4	33.3	32.0	—	33.3	—
Op.profit excl treasury gains	12,627	14,301	16,502	17,417	17,272	36.8	16,294	6.0
Key balance sheet items (Rs bn)								
Total deposits	1457	1498	1548	1674	1830			
Savings deposits	385	432	467	499	539			
Current deposits	270	322	333	372	362			
Term deposits	802	744	748	803	930			
CASA ratio (%)	45.0	50.3	51.7	52.0	49.2			
Loans	1038	1151	1196	1258	1462			
Retail credit	611	627	660	723	761			
Housing loans	62	64	77	87	95			
Car loans	161	171	180	197	214			
Loan against sec	7	8	8	9	10			
Personal loans	85	84	85	88	90			
Two wheeler	18	18	17	18	19			
Credit cards	38	38	38	38	39			
Commercial vehicles	77	79	84	94	100			
Business Banking	122	122	127	139	144			

Source: Company, Kotak Institutional Equities estimates

HDFC Bank-- key parameters and balance sheet
March fiscal year-ends, 1QFY10-1QFY11

	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11
Yield management measures (%)					
NIM	4.1	4.2	4.3	4.4	4.3
Asset quality details					
Gross NPL(Rs mn)	21,635	20,269	19,741	18,168	17,912
Gross NPL (%)	2.1	1.8	1.6	1.4	1.2
Net NPLs (Rs mn)	6,585	6,024	5,440	3,921	4,125
Net NPL (%)	0.6	0.5	0.4	0.3	0.3
Capital adequacy ratios (%)					
CAR	15.4	15.7	18.3	17.4	16.3
Tier I	10.6	10.9	13.8	13.3	12.4
Tier II	4.8	4.8	4.5	4.1	3.9
Other key details					
Branches	1,416	1,506	1,725	1,725	1,725
ATM network	3,382	3,573	3,898	4,232	4,393
Cities covered	550	635	771	779	780
Balance sheet snapshot (Rs bn)					
CAPITAL AND LIABILITIES					
Capital	4	4	5	5	5
Reserves and surplus	153	161	206	211	221
Deposits	1,457	1,498	1,548	1,674	1,830
Borrowings	30	51	76	66	52
Subordinated debt	64	64	64	64	63
Other liabilities and provisions	152	162	147	206	162
Total	1,862	1,940	2,046	2,225	2,333
ASSETS					
Cash and balances with RBI	118	137	112	155	149
Balances with banks, money at call and short notice	19	14	17	145	33
Investments	603	572	641	586	608
Advances	1,038	1,137	1,196	1,258	1,462
Fixed assets	20	20	21	21	22
Other assets	64	61	59	60	58
Total	1,861	1,939	2,046	2,225	2,333

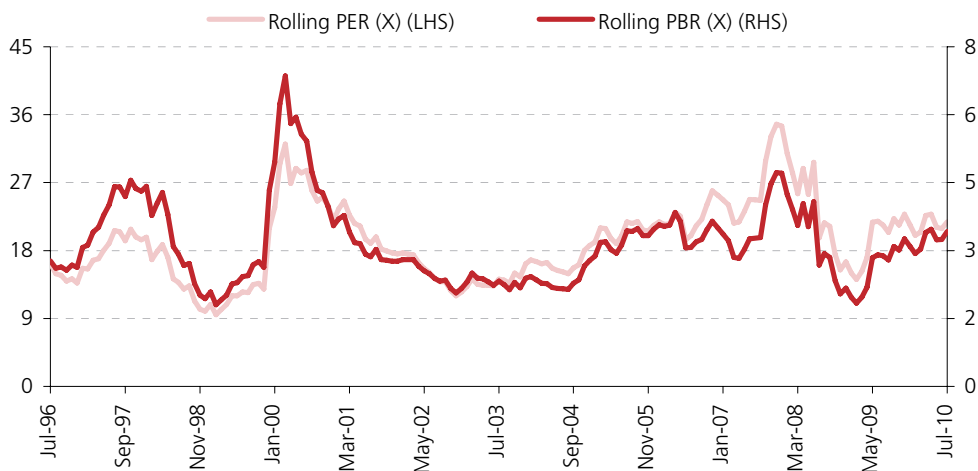
Source: Company

HDFC Bank—estimate changes
March fiscal year-ends, 2011-2012E, Rs bn

	Old estimates		New estimates		% change	
	2011E	2012E	2011E	2012E	2011E	2012E
Net loan growth (%)	25.0	25.1	27.2	25.1		
Retail loan to total loans (%)	47.8	41.6	47.0	40.9		
Total assets	2,568	3,160	2,709	3,331	5.5	5.4
Total income	137.8	167.2	143.2	172.3	3.9	3.1
Net interest income	92.8	111.9	100.7	121.5	8.5	8.6
NIM (%)	4.0	4.0	4.2	4.1		
Other income	45.1	55.2	42.5	50.7	(5.6)	(8.2)
Fee income	35.4	43.6	33.7	40.0	(4.9)	(8.3)
Expenses	67.0	77.0	66.2	77.2	(1.2)	0.2
Employee cost	25.9	29.8	26.9	32.2	3.9	7.8
Other cost	41.2	47.1	39.4	45.0	(4.4)	(4.6)
Loan loss provisions	14.2	17.7	16.4	20.7	16.1	17.0
PBT	69.3	88.2	57.0	74.4	(17.7)	(15.6)
PAT	39.0	50.7	39.9	52.1	2.5	2.7
PBT-treasury+provisions	82.0	103.9	75.5	93.4	(7.9)	(10.1)
EPS (Rs)	86.2	112.2	87.2	113.8	1.2	1.4
BVPS (Rs)	539.4	626.7	538.4	627.4	(0.2)	0.1

Source: Company, Kotak Institutional Equities estimates

Rolling PER and PBR (X) for HDFC Bank
July 1996-July 2010



Source: Kotak Institutional Equities

HDFC Bank growth rates and key ratios
 March fiscal year-ends, 2008-2013E (%)

	2008	2009	2010	2011E	2012E	2013E
Growth rates (%)						
Net loan	35.1	55.9	27.3	27.2	25.1	25.0
Customer assets growth	26.5	40.4	26.8	26.9	24.8	24.8
Retail loans to Customer assets	54.9	60.9	56.8	47.0	40.9	27.1
Net fixed assets	21.6	44.6	24.5	(3.5)	0.3	(2.1)
Cash and bank balance	61.4	18.5	71.0	(6.2)	11.0	11.9
Total Asset	46.0	37.6	21.4	21.8	23.0	22.6
Deposits	47.5	41.7	17.2	23.9	26.2	25.0
Current	45.2	(1.1)	30.9	11.4	19.9	25.0
Savings	33.5	73.3	1.1	29.2	28.7	25.0
Fixed	58.7	33.5	42.9	24.8	26.2	25.0
Net interest income	48.7	34.5	13.0	20.0	20.7	25.1
Loan loss provisions	41.2	42.0	12.3	(15.2)	26.0	19.6
Total other income	50.4	44.2	15.7	11.7	19.3	17.4
Net fee income	32.7	43.3	15.2	18.9	18.8	18.6
Net capital gains	(453.4)	58.2	(9.8)	(56.5)	16.7	—
Net exchange gains	48.7	111.4	2.0	16.0	20.0	15.0
Operating expenses	54.7	47.7	4.2	14.9	16.5	15.8
Employee expenses	67.5	72.0	2.3	17.4	19.7	18.4
Key ratios (%)						
Yield on average earning assets	9.7	10.8	8.3	8.4	8.7	8.9
Yield on average loans	12.6	15.0	10.8	10.6	10.8	10.9
Yield on average investments	7.9	7.4	6.8	7.0	7.2	7.3
Average cost of funds	5.2	6.7	4.6	4.8	5.2	5.4
Interest on deposits	5.2	6.6	4.5	4.7	5.1	5.2
Difference	4.6	4.1	3.7	3.6	3.5	3.6
Net interest income/earning assets	5.1	4.9	4.3	4.2	4.1	4.2
Spreads on lending business	7.5	8.3	6.2	5.8	5.6	5.6
Spreads on lending business (incl. Fees)	10.6	11.3	8.7	8.1	7.8	7.7
New provisions/average net loans	2.2	2.1	1.7	1.2	1.2	1.1
Total provisions/gross loans	1.0	1.0	1.1	1.9	2.5	2.9
Interest income/total income	70.7	69.3	68.8	70.3	70.6	71.9
Other income / total income	29.3	30.7	31.2	29.7	29.4	28.1
Fee income to total income	22.0	22.9	23.2	23.5	23.2	22.4
Fee income to advances	3.1	3.0	2.5	2.4	2.2	2.1
Fees income to PBT	75.2	74.5	66.0	59.0	53.7	48.6
Net trading income to PBT	(2.0)	11.6	8.0	(0.9)	2.4	1.8
Exchange inc./PBT	12.4	18.1	14.2	12.4	11.4	10.0
Operating expenses/total income	48.0	51.7	47.3	46.3	44.8	42.2
Operating expenses/assets	3.3	3.5	2.8	2.7	2.6	2.4
Operating profit /AWF	1.9	1.9	2.0	2.3	2.5	2.6
Tax rate	30.3	32.0	31.3	30.0	30.0	30.0
Dividend payout ratio	18.9	18.9	18.6	18.6	18.6	18.6
Share of deposits						
Current	28.5	19.9	22.2	20.0	19.0	19.0
Fixed	45.5	55.6	48.0	50.0	51.0	51.0
Savings	26.0	24.4	29.8	30.0	30.0	30.0
Loans-to-deposit ratio	62.9	69.2	75.2	77.1	76.5	76.5
Equity/assets (EoY)	8.6	8.2	9.7	9.1	8.6	8.3
Dupont analysis (%)						
Net interest income	4.7	4.7	4.1	4.1	4.0	4.1
Loan loss provisions	1.1	1.1	1.0	0.7	0.7	0.7
Net other income	2.0	2.1	1.9	1.7	1.7	1.6
Operating expenses	3.6	3.6	2.9	2.7	2.6	2.4
Invt. depreciation	—	—	—	0.1	—	—
(1- tax rate)	69.7	68.0	68.7	70.0	70.0	70.0
ROA	1.4	1.4	1.5	1.6	1.7	1.8
Average assets/average equity	12.5	11.9	11.1	10.7	11.3	11.8
ROE	17.7	16.9	16.1	17.3	19.5	21.8

Source: Company, Kotak Institutional Equities estimates

HDFC Bank P&L and balance sheet

March fiscal year-ends, 2008-2013E (Rs mn)

	2008	2009	2010	2011E	2012E	2013E
Income statement						
Total interest income	104,034	163,323	161,729	199,931	256,051	323,896
Loans	69,667	121,368	120,983	150,852	193,765	245,743
Investments	31,604	40,080	39,813	46,758	60,211	76,171
Cash and deposits	2,762	1,876	933	2,321	2,074	1,982
Total interest expense	48,871	89,111	77,863	99,268	134,522	171,820
Deposits from customers	43,827	80,155	69,977	87,246	119,089	153,203
Net interest income	55,163	74,212	83,866	100,663	121,529	152,076
Loan loss provisions	12,160	17,263	19,391	16,437	20,708	24,763
Net interest income (after prov.)	43,002	56,949	64,475	84,226	100,821	127,313
Other income	22,825	32,906	38,077	42,537	50,730	59,552
Net fee income	17,145	24,573	28,306	33,658	39,985	47,432
Net capital gains	2,418	3,826	3,451	1,500	1,750	1,750
Net exchange gains	2,831	5,986	6,103	7,079	8,495	9,770
Operating expenses	37,456	55,328	57,645	66,235	77,153	89,316
Employee expenses	13,014	22,382	22,892	26,868	32,153	38,085
Depreciation on investments	2,884	—	—	2,000	—	—
Other Provisions	2,683	1,528	2,010	1,500	—	—
Pretax income	22,811	32,999	42,898	57,028	74,399	97,549
Tax provisions	6,909	10,549	13,410	17,108	22,320	29,265
Net Profit	15,902	22,449	29,488	39,920	52,079	68,284
% growth	39.3	41.2	31.4	35.4	30.5	31.1
Operating profit	35,229	47,964	60,847	75,465	93,357	120,561
% growth	33.8	36.1	26.9	24.0	23.7	29.1
Balance sheet						
Cash and bank balance	147,783	175,066	299,424	280,875	311,813	348,808
Cash	9,401	15,862	24,353	26,788	29,467	32,413
Balance with RBI	116,131	119,410	130,480	109,496	137,755	171,804
Balance with banks	9,949	9,051	7,092	7,092	7,092	7,092
Net value of investments	493,933	588,252	586,154	746,407	935,410	1,149,720
Govt. and other securities	316,656	521,566	510,499	671,224	860,227	1,074,537
Shares	345	397	1,035	1,035	1,035	1,035
Debentures and bonds	62,517	19,428	11,393	11,393	11,393	11,393
Net loans and advances	634,269	988,830	1,258,306	1,600,237	2,001,150	2,501,196
Fixed assets	11,751	16,989	21,150	20,410	20,472	20,040
Net leased assets	—	—	—	—	—	—
Net Owned assets	11,751	16,989	21,150	20,410	20,472	20,040
Other assets	44,027	63,568	59,551	60,983	62,558	64,291
Total assets	1,331,764	1,832,706	2,224,586	2,708,912	3,331,403	4,084,054
Deposits	1,007,686	1,428,116	1,674,044	2,074,359	2,617,012	3,270,949
Borrowings and bills payable	108,852	120,860	188,414	226,163	248,688	275,719
Other liabilities	100,254	133,257	146,902	161,945	178,527	196,808
Total liabilities	1,216,792	1,682,233	2,009,361	2,462,467	3,044,228	3,743,476
Paid-up capital	3,544	4,254	4,577	4,577	4,577	4,577
Reserves & surplus	111,428	146,219	210,648	241,868	282,597	336,001
Total shareholders' equity	114,972	150,473	215,225	246,445	287,175	340,578

Source: Company, Kotak Institutional Equities estimates

JULY 20, 2010
RESULT

Coverage view: **Cautious**

Price (Rs): **348**

Target price (Rs): **420**

BSE-30: **17,928**

Good quarter, though sales volumes disappoint a bit. Sesa's 1QFY11 results were in line with our expectations; EBITDA grew 222% yoy and declined 2.9% qoq to Rs14.6 bn. Net income grew 208% yoy and 7.3% qoq to Rs13 bn. Iron ore sales volumes were a touch below our expectations. Spot iron prices have declined 32% over the past two months on mounting concerns of a slowdown in China. We will review our estimates after the earnings call. Maintain REDUCE rating.

Company data and valuation summary

Sesa Goa

Stock data

52-week range (Rs) (high,low) 495-208

Market Cap. (Rs bn) 309.9

Shareholding pattern (%)

Promoters 57.0

FIs 26.6

MFs 0.3

Price performance (%)

Absolute 1M 3M 12M (1.5) (24.2) 59.5

Rel. to BSE-30 (3.5) (26.4) 31.2

Forecasts/Valuations

2010 2011E 2012E

EPS (Rs) 29.6 61.4 62.4

EPS growth (%) 32.2 107.6 1.8

P/E (X) 11.8 5.7 5.6

Sales (Rs bn) 58.6 112.4 116.9

Net profits (Rs bn) 26.3 54.6 55.5

EBITDA (Rs bn) 31.4 74.0 73.1

EV/EBITDA (X) 9.6 3.4 2.8

ROE (%) 36.7 48.0 34.1

Div. Yield (%) 0.9 0.9 0.9

In-line quarter; sales tonnage lower than expected

Sesa reported 1QFY11 net profit of Rs13 bn (+208.3% yoy and +7.3% qoq)—ahead of our expectation of Rs11.7 bn. We attribute this variance to below-EBITDA line items i.e. higher-than-expected other income and lower-than-expected tax provisions. Note that yoy performance is not comparable since Dempo acquisition has been consolidated only from Sep' 09 quarter. EBITDA of Rs14.6 bn in line with our expectation of Rs14.63 bn.

Iron ore realization of US\$91/ ton was ahead of our expectation. Sales volumes were 5.4 mn tons; adjusted for Dempo volumes of 1.2 mn tons, sales volumes declined on a yoy basis. The company attributes relatively weak tonnage performance to forest permit related issues in Karnataka and logistics constraints in Orissa. We would seek clarifications/comfort regarding the company's 20-25% volume growth target against the backdrop of these concerns and potentially weak offtake of low grade ore by Chinese traders

Iron ore prices likely to decline further; mainly led by the incremental slowdown in China

Iron ore spot prices (63% Fe China CFR) have declined 32% from the recent peak. Weaker demand in China is the principle cause as a rapid softening in steel prices has forced many smaller mills to curtail output. China's transition to lower growth will likely have an impact across the steel sector and consequently iron ore market. We expect iron ore prices to trend lower in the near term as well as over the next few years as demand imbalances become smaller and new projects by mining majors come on stream.

We will review our earnings estimates after the quarterly earnings call

We will review our earnings estimates post results earnings call, especially on volume growth guidance. Our realization assumptions of US\$92/ ton for FY2011E and US\$83/ ton for FY2012E may prove optimistic. On an interesting note, the discount of 58% FE content ore has widened considerably, to 28.4% from an average of 18% over the past 12 months. Sesa's seemingly inexpensive valuations have to be viewed against the backdrop of relatively low mine life and weak quality iron ore content.

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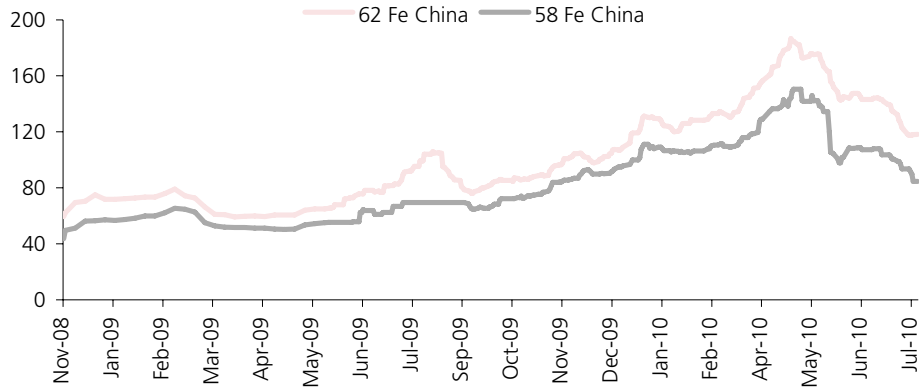
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Interim results of Sesa Goa, March fiscal year-ends (Rs mn)

	1QFY11	1QFY11E	1QFY10	4QFY10	(% chg.)		
					1QFY11E	1QFY10	4QFY10
Net sales	23,940	24,659	9,986	24,035	(2.9)	139.7	(0.4)
Total expenditure	(9,535)	(10,188)	(5,584)	(9,159)	(6.4)	70.7	4.1
(Inc)/Dec in stock	1,392	—	(180)	639	—	(873.4)	117.9
Consumption of raw materials	(855)	(1,089)	(814)	(881)	(21.5)	5.0	(3.0)
Staff costs	(444)	(470)	(395)	(447)	(5.4)	12.6	(0.6)
Stores	(737)	(725)	(535)	(686)	1.7	37.7	7.5
Inland transportation cost	(2,556)	(2,983)	(2,262)	(2,417)	(14.3)	13.0	5.8
Other transportation services	(901)	(1,417)	(659)	(1,232)	(36.4)	36.7	(26.9)
Purchase of ore	(1,471)	(1,197)	(273)	(1,621)	22.8	438.6	(9.2)
Export tax	(1,276)	(1,151)	(39)	(1,215)	10.8	3,146.3	5.0
Other expenditure	(2,774)	(1,155)	(502)	(1,444)	140.0	452.8	92.0
Expenses recovered	87	—	75	145	—	17.0	(39.7)
Other operating income	190	154	129	154	24.0	47.5	24.0
EBITDA	14,596	14,625	4,531	15,030	(0.2)	222.1	(2.9)
OPM (%)	61	59	45	63			
Other income	1,609	949	752	1,291	69.6	114.2	24.7
Interest	(137)	—	(20)	(227)	—	576.8	(39.3)
Depreciation	(191)	(186)	(152)	(166)	2.8	26.1	15.0
Pretax profits	15,877	15,388	5,110	15,928	3.2	210.7	(0.3)
Extraordinaries							
Tax	(2,832)	(3,693)	(869)	(3,777)	(23.3)	225.7	(25.0)
Net income before minority interest	13,045	11,695	4,241	12,151	11.5	207.6	7.4
Minority interest	(27)	(23)	(18)	(22)	17.8	49.7	21.0
PAT after minority interest	13,018	11,672	4,223	12,129	11.5	208.3	7.3
Income tax rate (%)	17.8	24.0	17.0	23.7	—	—	—
Ratios							
EBITDA margin (%)	61.0	59.3	45.4	62.5	2.8	34.4	(2.5)
ETR (%)	17.8	24.0	17.0	23.7	(25.7)	4.8	(24.8)
EPS (Rs)	15.2	14.9	5.4	15.4	2.1	181.7	(1.7)
Volume details ('000 tons)							
Iron ore sales	5,442	5,736	4,736	7,375	(5.1)	14.9	(26.2)
Pig iron	54	70	71	70	—	(23.9)	(22.9)
Realization (US\$/ ton)							
Iron ore	91.3	83.0	37.1	66.6	10.0	146.0	37.0
Iron ore EBITDA	59.7	51.6	17.2	42.5	15.6	246.5	40.3
Segmental revenues (Rs mn)	25,213	24,659	10,891	25,132	2.2	131.5	0.3
Iron ore	22,685	21,724	8,557	22,602	4.4	165.1	0.4
Metallurgical coke	1,160	1,081	1,008	1,029	7.4	15.1	12.7
Pig iron	1,368	1,855	1,326	1,501	(26.3)	3.2	(8.9)
Segmental PBIT (Rs mn)	15,335	15,388	4,386	14,900	(0.3)	249.6	2.9
Iron ore	14,744	14,618	3,926	14,511	0.9	275.6	1.6
Metallurgical coke	281	308	254	122	(8.7)	10.5	129.5
Pig iron	310	462	207	267	(32.9)	50.0	16.2
Segmental PBIT margins (%)	61	62	40	59			
Iron ore	65.0	67.3	45.9	64.2	(3.4)	41.7	1.2
Metallurgical coke	24.2	28.5	25.2	11.9	(15.0)	(4.0)	103.6
Pig iron	22.7	24.9	15.6	17.8	(9.0)	45.4	27.4

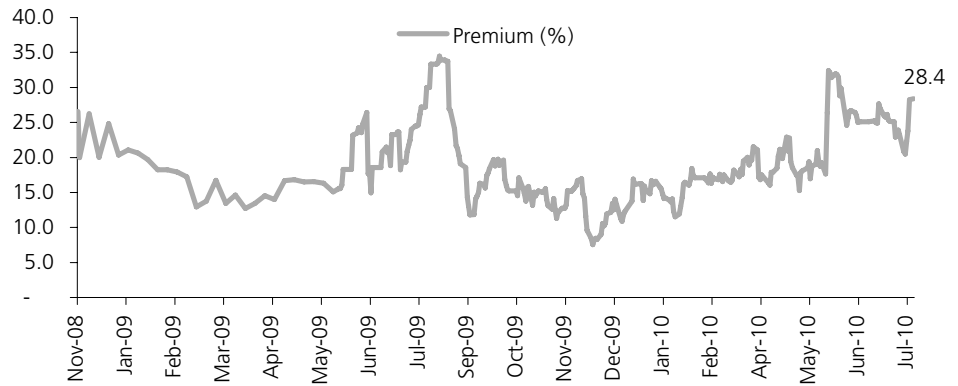
Source: Company, Kotak Institutional Equities estimates

Gap between low grade and high grade iron ore has expanded considerably
China 62 & 58 Fe comparison, December year ends, 2008-2010 (US\$/ton)



Source: Bloomberg, Kotak Institutional Equities estimates

Discount of 58% Fe iron ore has increased considerably over the benchmark, December year-ends. 2008-2010 (%)



Source: Bloomberg, Kotak Institutional Equities estimates

JULY 20, 2010

RESULT

Coverage view: **Attractive**

Price (Rs): **1,415**

Target price (Rs): **1,320**

BSE-30: **17,928**

Revenue disappointment likely led by lower-than-expected volume growth.

Concor reported weaker-than-expected revenues of Rs9.2 bn, relatively flat on a yoy basis, missing our estimates by about 6% likely led by a lower-than-expected pick-up in volumes. Margins at 27% were about 50 bps below our estimate leading to a net PAT disappointment of 9% (PAT at Rs1.9 bn, down 3.7% yoy). Exim margins remained stable; however, domestic segment recorded sharp margin contraction. Retain REDUCE.

Company data and valuation summary

Container Corporation

Stock data

52-week range (Rs) (high,low)	1,500-956
Market Cap. (Rs bn)	183.9

Shareholding pattern (%)

Promoters	63.1
FIs	23.4
MFs	4.3

Price performance (%)

	1M	3M	12M
Absolute	10.9	5.0	46.6
Rel. to BSE-30	8.7	1.9	20.5

Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	61.1	74.3	85.9
EPS growth (%)	0.3	21.7	15.6
P/E (X)	23.2	19.0	16.5
Sales (Rs bn)	36.8	42.5	48.8
Net profits (Rs bn)	7.9	9.7	11.2
EBITDA (Rs bn)	10.1	12.2	14.0
EV/EBITDA (X)	16.4	13.4	11.2
ROE (%)	19.6	20.6	20.5
Div. Yield (%)	1.0	1.2	1.4

Revenue miss versus estimates likely to be led by lower-than-expected pick-up in volumes

Concor reported 1QFY11 revenues of Rs9.1 bn, relatively flat on a yoy basis and about 6% below our estimate of Rs9.7 bn (see Exhibit 1). The revenue disappointment is likely to have been led by a slower-than-expected pick-up in volumes. Exim revenues of Rs7.2 bn was about 6.3% below our estimate while domestic revenues of Rs1.95 bn was 3.7% below our estimate (see Exhibit 2). Our estimates were based on 10% yoy growth in volumes and flat realizations on a sequential basis.

Margins broadly in line; sharp decline in domestic segment margins

Concor reported marginal contraction of EBITDA margins on a yoy basis to 27% in 1QFY11 from 27.3% in 1QFY10. This is versus our margin assumption of 27%. The lower-than-expected revenues and slight miss on the margin level led to a net PAT disappointment of about 9% versus our estimates. Concor reported a PAT of Rs1.9 bn, down 3.7% yoy. PBIT margins for the exim segment expanded slightly, by 50 bps, on a yoy basis while the domestic segment PBIT margins recorded a sharp decline of 320 bps yoy and 250 bps on a sequential basis. The decline in margins might have been led by (1) hikes in rail freight charges not yet fully passed onto the customer and (2) drop in terminal service revenues which is a high EBITDA segment.

New SFTO policy broadens commodity base; but competition may diminish potential returns

The Ministry of Railways has come up with a new 'Special Freight Train Operator' scheme with an aim to increase the Railways' share in transportation by increasing the commodity base. Under this scheme, a train operator would have to invest in wagons and tie up with an end user. The operator would have to bid for license for a particular commodity type and would in return receive concessional freight rates from the Indian Railways. However, stiff competition may lead to aggressive bids and might diminish the potential returns for a rail operator. Concor is evaluating the option to run car-carriers through this scheme for its 50:50 JV company with NYK Line.

Reiterate REDUCE with a TP of Rs1,320; will revisit estimates post today's conference call

Retain estimates and REDUCE rating. We revise our TP to Rs1,320 (from Rs1,250) based on shift to FY2012E-based valuation. We will revisit our estimates post today's conference call at 11 am.

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Exhibit 1: Revenue disappointment likely led by lower-than-expected volume growth

Container Corporation - 1QFY11 results - key numbers (Rs mn)

	1QFY11	1QFY11E	1QFY10	4QFY10	% change			FY2011E	FY2010	%change
					1QFY11E	1QFY10	4QFY10			
Net Sales	9,159	9,720	9,074	9,505	(5.8)	0.9	(3.6)	42,489	37,023	14.8
Staff cost	(202)	(190)	(198)	(190)	6.4	2.5	6.4	(926)	(785)	17.9
Rail freight exp	(5,274)	(5,589)	(5,269)	(5,571)	(5.6)	0.1	(5.3)	(23,959)	(21,272)	12.6
Others	(1,213)	(1,264)	(1,129)	(1,543)	(4.0)	7.4	(21.4)	(5,799)	(5,203)	12.6
Total exp	(6,689)	(7,043)	(6,595)	(7,305)	(5.0)	1.4	(8.4)	(30,683)	(27,260)	13.8
EBITDA margin	2,470	2,677	2,478	2,201	(7.7)	(0.3)	12.2	11,805	9,763	20.9
Other Income	359	467	413	383	(23.2)	(13.0)	(6.2)	1,869	1,616	15.6
PBDIT	2,829	3,144	2,891	2,584	(10.0)	(2.2)	9.5	13,674	11,379	20.2
Depreciation	(352)	(421)	(316)	(365)	(16.2)	11.5	(3.4)	(1,682)	(1,343)	25.2
PBT	2,476	2,724	2,575	2,219	(9.1)	(3.8)	11.6	11,992	10,036	19.5
Tax	(541)	(599)	(566)	(487)	(9.7)	(4.4)	11.1	(2,332)	(2,245)	3.9
PAT	1,935	2,125	2,009	1,727	(8.9)	(3.7)	12.0	9,660	7,786	24.1
Key ratios (%)										
Rail freight exps/Sales	57.6	57.5	58.1	58.6				56.4	57.5	
Other exp/Sales	13.2	13.0	12.4	16.2				13.6	14.1	
Employee exp/Sales	2.2	2.0	2.2	2.0				2.2	2.1	
EBITDA margin	27.0	27.5	27.3	23.2				27.8	26.4	
PBT margin	27.0	28.0	28.4	23.3				28.2	27.1	
Effective tax rate	21.9	22.0	22.0	22.0				19.4	22.4	
PAT margin	21.1	21.9	22.1	18.2				22.7	21.0	

Source: Company, Kotak Institutional Equities estimates

Exhibit 2: Both exim and domestic revenues disappoint; sharp margin contraction in domestic segment

Container Corporation - 1QFY11 results - segmental key numbers (Rs mn)

Segmental	1QFY11	1QFY11E	1QFY10	4QFY10	% change			FY2011E	FY2010	%change
					1QFY11E	1QFY10	4QFY10			
Sales (Rs mn)										
Exim	7,202	7,687	7,243	7,257	(6.3)	(0.6)	(0.8)	33,126	28,953	14.4
(% of total)	78.6	79.1	79.8	76.3				78.0	78.2	
Domestic	1,957	2,033	1,831	2,249	(3.7)	6.9	(13.0)	9,363	8,069	16.0
(% of total)	21.4	20.9	20.2	23.7				22.0	21.8	
EBIT (Rs mn)										
Exim	1,986		1,961	1,603		1.3	23.9	8,172	7,561	8.1
Margin (%)	27.6		27.1	22.1				24.7	26.1	
Domestic	266		307	362		(13.4)	(26.5)	1,570	1,300	20.7
Margin (%)	13.6		16.8	16.1				16.8	16.1	

Source: Company, Kotak Institutional Equities estimates

Exhibit 3: Key features of the Special Freight Train Operator scheme of the railway ministry

Key eligibility criteria	Should be a registered company in India Minimum 3 years experience in transport & logistics or port & terminal operations or warehousing or container train operations or wagon leasing Minimum net worth of Rs500 mn
Bidding terms	Separate bid for each commodity category Winning bid decided on basis of a registration fee quoted by the participant Registration bid must be higher than the specified reserve price for that commodity Maximum 5 operators to be selected for each commodity type
Concession period	20 years, extendable till expiry of codal life of wagon
Freight rebate	12% on base freight for 20 years or recovery of cost whichever is earlier Additional rebate of 2% for each 10% increase additional tonnage beyond existing throughput (for High Capacity Wagons)
Other key features	Train operator to charge tariff from end user Minimum investment of 3 rakes Maintenance of wagons by Railways at its own cost except special components
Cargo categories	Category 1: Automobile, RO-RO traffic Category 2: Bulk fertilizers, bulk cement, fly ash Category 3: Bulk chemicals, petrochemicals, bulk alumina Category 4: Steel products requiring specially designed wagons Category 5: Molasses, edible oil, caustic soda

Source: Railway ministry, News flows

Exhibit 4: Key financials of Container Corporation, March fiscal year-ends, 2007-12E (Rs mn)

	2007	2008	2009	2010E	2011E	2012E
Income statement						
Net revenues	30,573	33,473	34,172	36,842	42,489	48,810
Total operating cost	(21,661)	(24,569)	(24,861)	(27,102)	(30,683)	(35,217)
EBIDTA	8,912	8,904	9,311	9,740	11,805	13,592
Other income	846	1,645	2,111	1,686	1,869	2,255
PBDIT	9,758	10,548	11,422	11,427	13,674	15,848
Depreciation	(936)	(1,063)	(1,159)	(1,450)	(1,682)	(1,888)
Pre tax profits	8,823	9,485	10,262	9,977	11,992	13,960
Tax	(1,862)	(1,980)	(2,347)	(2,038)	(2,332)	(2,791)
PAT	6,961	7,505	7,915	7,939	9,660	11,168
EPS (Rs)	54	58	61	61	74	86
One time items	77.4	16.9	(3.1)	-	-	-
PAT (reported)	7,038	7,522	7,912	7,939	9,660	11,168
Volume handled ('000 TEUs)						
Exim	1,716	1,977	1,855	1,874	2,061	2,267
Domestic	58	71	453	521	584	642
Balance sheet						
Networth	26,298	31,839	37,622	43,425	50,485	58,648
Share capital	650	650	1,300	1,300	1,300	1,300
Reserves & surplus	25,648	31,189	36,322	42,125	49,185	57,348
Total sources of funds	26,298	31,839	37,622	43,425	50,485	58,648
Net block	15,515	16,652	19,490	25,214	28,673	30,271
CWIP	2,028	1,721	2,457	818	818	818
Investments	1,317	1,554	2,031	3,031	4,031	5,031
Net current assets	9,051	13,650	15,582	16,300	18,901	24,466
Net deferred tax asset	(1,613)	(1,737)	(1,938)	(1,938)	(1,938)	(1,938)
Total application of funds	26,298	31,839	37,622	43,425	50,485	58,648

Source: Company, Kotak Institutional Equities estimates

JULY 20, 2010

RESULT

Coverage view: **Attractive**

Price (Rs): **270**

Target price (Rs): **290**

BSE-30: **17,928**

1Q broadly in line; international subsidiaries look up; power disappoints.

Consolidated revenues of Rs23 bn was in line with our estimates. Standalone revenue growth of 14.4% and likely subsidiary growth of 6.5% (adj. for currency movement) is broadly in line with management's full-year guidance. Industrial and consumer segments continued to record very strong growth; however, sedate power segment numbers are disappointing. Reiterate BUY; will revisit estimates post today's conference call.

Company data and valuation summary

Crompton Greaves

Stock data	Forecasts/Valuations		
	2010	2011E	2012E
52-week range (Rs) (high,low)	280-149		
Market Cap. (Rs bn)	173.3		
Shareholding pattern (%)			
Promoters	40.9		
FIs	16.0		
MFs	18.4		
Price performance (%)			
	1M	3M	12M
Absolute	6.8	2.3	56.3
Rel. to BSE-30	4.6	(0.7)	28.5
EPS (Rs)	12.8	13.2	15.7
EPS growth (%)	46.5	2.9	19.0
P/E (X)	21.0	20.4	17.2
Sales (Rs bn)	91.4	98.3	113.5
Net profits (Rs bn)	8.2	8.5	10.1
EBITDA (Rs bn)	12.8	13.2	15.4
EV/EBITDA (X)	13.0	12.2	10.1
ROE (%)	37.9	29.6	27.7
Div. Yield (%)	0.5	0.7	0.8

Revenue in line; slight margin surprise leads to higher-than-expected PAT

- ▶ **Revenues – in line with estimates and full-year company guidance.** Crompton reported 1QFY11 revenues of Rs23 bn, up about 5% on a yoy basis, in line with our estimate. The standalone entity reported a strong revenue growth of 14.4% yoy while the subsidiary revenues declined by about 6.3% yoy (likely growth of +6.5% adjusted for currency movement). These results are broadly in line with the management's guidance of 15% yoy standalone revenue growth and 5% growth for the subsidiaries in local currency terms. EBITDA margin at 12.9% was 90 bps higher than our estimate of 12%. The higher-than-expected margins led to a PAT of Rs1.9 bn, up 18% yoy and about 8% higher than our estimate of Rs1.75 bn.
- ▶ **International subsidiaries may have recorded a positive revenue growth - adjusted for currency movement.** Crompton reported a 6.3% yoy decline in subsidiary revenues to Rs9.6 bn in 1QFY11. However, highlight that the average EUR-INR rate in 1QFY11 was about 12.8% lower at 58 versus 66.5 in 1QFY10. Hence, this implies that the revenues of the international subsidiaries have actually recorded a 6.5% yoy growth in Euro terms.
- ▶ **Very strong industrial and consumer segment number; but power segment disappoints.** Crompton's standalone revenue growth was primarily led by very strong consumer and industrial segments which recorded 28.8% and 22.6% yoy growth, respectively. The power revenues remained relatively flat on a yoy basis at the consolidated as well as standalone levels, which was a bit of a disappointment. We expected power segment to report about 14-15% growth at the standalone level.

Reiterate BUY with a TP of Rs290; will revisit estimates post today's conference call

We retain our estimates of Rs13.2 and Rs15.7 for FY2011E and FY2012E and target price of Rs290/share. Reiterate BUY on (1) strong domestic growth potential, (2) margin contraction and Europe exposure risks are more contained vs perception, (3) strong cash flow generation, (4) likely recovery in industrial capex and (5) expected robust XII plan T&D spending. We will revisit our estimates post today's conference call scheduled at 6 pm.

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Revenue in line; slight margin surprise leads to higher-than-expected PAT

Crompton reported consolidated revenues of Rs23 bn in 1QFY11, up 5% yoy from Rs22 bn in 1QFY10 – in line with our estimates. The consolidated margins expanded by 160 bps yoy to 12.9% versus our estimate of 12% EBITDA margin. The margin expansion was primarily led by lower other expenses as a percentage of sales which declined by about 140 bps yoy to 12.5% of sales in this quarter versus 13.9% in 1QFY10. The other expenses have also recorded a yoy decline on an absolute basis by about 6%. The better-than-expected margins led to a PAT of Rs1.9 bn, up 18% yoy and about 8% higher than our estimate of Rs1.75 bn.

Crompton Greaves - 1QFY11 consolidated revenue model (Rs mn)

	1QFY11	1QFY11E	1QFY10	4QFY10	% change			FY2011E	FY2010	% chg.
					1QFY11E	1QFY10	4QFY10			
Sales	23,022	23,099	21,975	25,079	(0.3)	4.8	(8.2)	98,292	91,409	7.5
Expenses	(20,049)	(20,327)	(19,499)	(21,052)	(1.4)	2.8	(4.8)	(85,056)	(78,639)	8.2
Stock	891		315	(1,025)		182.4	(186.9)	-	(225)	(100.0)
Raw material	(15,074)		(13,894)	(14,757)		8.5	2.1	(61,123)	(55,698)	9.7
Employee	(2,994)		(2,865)	(2,621)		4.5	14.2	(12,138)	(11,131)	9.0
Other Exp	(2,871)		(3,055)	(2,650)		(6.0)	8.4	(11,795)	(11,585)	1.8
EBITDA	2,973	2,772	2,476	4,027	7.3	20.1	(26.2)	13,236	12,770	3.7
Other income	183	278	239	329	(34.1)	(23.4)	(44.4)	1,110	937	18.5
PBDIT	3,156	3,049	2,715	4,356	3.5	16.2	(27.5)	14,346	13,706	4.7
Interest	(50)	(89)	(45)	(119)	(43.8)	11.1	(57.9)	(357)	(265)	34.6
Depreciation	(415)	(384)	(371)	(397)	8.1	11.8	4.6	(1,536)	(1,551)	(1.0)
PBT	2,691	2,576	2,299	3,840	4.5	17.1	(29.9)	12,454	11,891	4.7
Tax	(794)	(824)	(695)	(1,138)	(3.7)	14.3	(30.3)	(3,980)	(3,650)	9.0
Net profit	1,897	1,752	1,605	2,702	8.3	18.2	(29.8)	8,474	8,241	2.8
Key ratios (%)										
Raw material/Sales	61.6		61.8	62.9				62.2	61.2	
Employee exp./Sales	13.0		13.0	10.5				12.3	12.2	
Other exp./Sales	12.5		13.9	10.6				12.0	12.7	
EBITDA margin	12.9	12.0	11.3	16.1				13.5	14.0	
PBT Margin	11.7	11.2	10.5	15.3				12.7	13.0	
Tax rate	29.5	32.0	30.2	29.6				32.0	30.7	
PAT margin	8.2	7.6	7.3	10.8				8.6	9.0	

Source: Company, Kotak Institutional Equities estimates

Strong growth at standalone level

Crompton reported standalone revenues of Rs13.4 bn in 1QFY11, up 14.4% yoy from Rs11.7 bn in 1QFY10. Standalone operating margin for 1QFY11 expanded by about 80 bps yoy to 15.6% from 14.8% in 1QFY10. Strong revenue growth and margin expansion led to a PAT of Rs1.4 bn in 1QFY11, up 24% yoy, from Rs1.1 bn in 1QFY10.

Crompton Greaves - 1QFY11 standalone revenue model (Rs mn)

	1QFY11	1QFY10	4QFY10	% change		FY2011E	FY2010	% chg.
				1QFY10	4QFY10			
Sales	13,429	11,735	16,182	14.4	(17.0)	62,073	52,840	17.5
Expenses	(11,335)	(9,994)	(13,475)	13.4	(15.9)	(52,469)	(44,262)	18.5
Stock	1,067	486	(636)	119.5	(267.8)			
Raw material	(10,171)	(8,357)	(10,400)	21.7	(2.2)	(37,244)	(35,247)	5.7
Employee	(726)	(630)	(650)	15.2	11.7	(2,238)	(2,558)	(12.5)
Other Exp	(1,505)	(1,493)	(1,790)	0.8	(15.9)	(12,987)	(6,458)	101.1
EBITDA	2,094	1,740	2,707	20.3	(22.7)	9,604	8,578	12.0
Other income	148	84	337	75.1	(56.1)	857	688	24.6
PBDIT	2,242	1,825	3,044	22.8	(26.4)	10,461	9,265	12.9
Interest	6	6	(38)	6.8	(116.7)	(198)	(44)	356.1
Depreciation	(172)	(128)	(129)	34.4	33.3	(528)	(519)	1.8
PBT	2,075	1,702	2,877	21.9	(27.9)	9,735	8,703	11.9
Tax	(654)	(555)	(970)	17.8	(32.6)	(3,232)	(2,933)	10.2
Net profit	1,422	1,147	1,907	23.9	(25.5)	6,503	5,770	12.7
Key ratios (%)								
Raw material/Sales	67.8	67.1	64.3			60.0	66.7	
Employee exp./Sales	5.4	5.4	4.0			3.6	4.8	
Other exp./Sales	11.2	12.7	11.1			20.9	12.2	
EBITDA margin	15.6	14.8	16.7			15.5	16.2	
PBT Margin	15.5	14.5	17.8			15.7	16.5	
Tax rate	31.5	32.6	33.7			33.2	33.7	
PAT margin	10.6	9.8	11.8			10.5	10.9	

Source: Company, Kotak Institutional Equities estimates

Yoy decline in subsidiary revenues; but likely to have grown in local currency terms

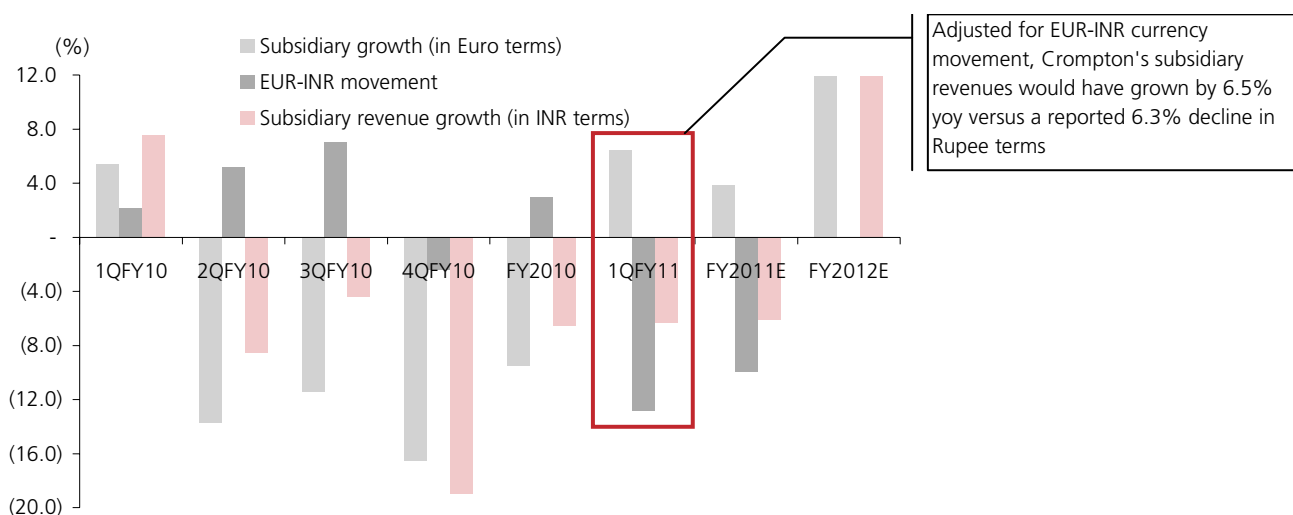
Crompton reported a 6.3% yoy decline in subsidiary revenues to Rs9.6 bn in 1QFY11 from Rs10.2 bn in 1QFY10. However, the average EUR-INR rate in 1QFY11 was about 12.8% lower at 58 versus 66.5 in 1QFY10. Hence, this implies that the revenues of the international subsidiaries have actually recorded a 6.5% yoy growth in Euro terms. We believe this could be a reflection of some revival in the demand scenario of the international markets. The subsidiary order inflow numbers for the quarter would be a key factor to watch for which would be another key indicator of the environment in the international markets. At the PAT level, the subsidiaries reported a growth of 4% yoy - growth led by margin expansion of 200 bps yoy was partially offset by lower other income.

Crompton Greaves - 1QFY10 subsidiary numbers (Rs mn)

	1QFY11	1QFY10	4QFY10	% change		FY2011E	FY2010	% chg.
				1QFY10	4QFY10			
Sales	9,593	10,241	8,897	(6.3)	7.8	36,219	38,569	(6.1)
Expenses	(8,713)	(9,504)	(7,577)	(8.3)	15.0	(32,587)	(34,377)	(5.2)
Stock	(176)	(170)	(389)	3.2	(54.8)	-	(718)	(100.0)
Raw material	(4,903)	(5,537)	(4,357)	(11.5)	12.5	(23,879)	(19,959)	19.6
Employee	(2,268)	(2,235)	(1,971)	1.5	15.1	(9,901)	(8,574)	15.5
Other Exp	(1,367)	(1,562)	(860)	(12.5)	58.9	1,192	(5,127)	(123.3)
Operating profit	880	736	1,320	19.5	(33.3)	3,631	4,192	(13.4)
Other income	35	155	(7)	(77.2)	(582.2)	254	249	1.7
EBIDT	915	891	1,312	2.7	(30.3)	3,885	4,441	(12.5)
Interest	(56)	(51)	(81)	10.6	(30.7)	(158)	(221)	(28.5)
Depreciation	(243)	(243)	(268)	(0.1)	(9.3)	(1,008)	(1,032)	(2.3)
PBT	616	597	963	3.2	(36.1)	2,719	3,188	(14.7)
Tax	(140)	(140)	(168)	0.4	(16.8)	(748)	(717)	4.3
Net profit	476	457	795	4.0	(40.2)	1,971	2,471	(20.2)
Key ratios (%)								
Raw material/Sales	51.1	54.1	49.0			65.9	51.7	
Employee exp./Sales	23.6	21.8	22.2			27.3	22.2	
Other exp./Sales	14.2	15.3	9.7			(3.3)	13.3	
EBITDA margin	9.2	7.2	14.8			10.0	10.9	
PBT Margin	6.4	5.8	10.8			7.5	8.3	
Tax rate	22.8	23.4	17.5			27.5	22.5	
PAT margin	5.0	4.5	8.9			5.4	6.4	

Source: Company, Kotak Institutional Equities estimates

Quarterly subsidiary revenues of Crompton in local currency and INR terms



Source: Company, Bloomberg, Kotak Institutional Equities estimates

Results broadly in line with management's full-year guidance for FY2011E

The 1QFY11 revenues are broadly in line with the management's full-year revenue guidance of 15% growth at the standalone business (reported 14.4% yoy growth) and 5% growth in the international subsidiary revenue in local currency terms (likely to be about 6-6.5% growth in 1QFY11E).

Strong industrial and consumers segment numbers; power segment disappoints

The strong growth trend of industrials and consumer segments seen in the past few quarters continued in 1QFY11 as well. At the standalone level, industrial segment revenues grew by 22.6% yoy to Rs3.1 bn while consumer segment grew by 28.8% yoy to Rs5.3 bn. This is in line with the trend seen in the product segment revenues for several companies such as ABB, Siemens etc. in 2HFY10. We believe that this is a harbinger of pick-up in industrial capex activity and expect these segments to record strong growth going forward as well.

Disappointing power segment revenues

The power segment revenues of Crompton remained relatively flat at Rs5.1 bn in 1QFY11 at the standalone level. This was a bit of a disappointment - we had expected standalone power business to report a growth of about 15% on a yoy basis. Part of the slowdown in the power revenues may be led by a slowdown in the export revenues of the standalone entity. Power segment revenues declined by about 1.8% yoy on a consolidated basis implying a 3% yoy decline in subsidiary power business. However, adjusted for the EUR-INR currency movement, subsidiary power segment might have recorded a 9-10% yoy growth.

Segment-wise standalone and consolidated revenues and EBIT for Crompton (Rs mn)

	Consolidated					Standalone				
	1QFY11	1QFY10	4QFY10	%change		1QFY11	1QFY10	4QFY10	%change	
				1QFY10	4QFY10				1QFY10	4QFY10
Revenues						Revenues				
Power Systems	14,564	14,838	16,838	(1.8)	(13.5)	5,101	5,084	8,286	0.3	(38.4)
Consumer Products	5,318	4,129	4,604	28.8	15.5	5,318	4,129	4,604	28.8	15.5
Industrial systems	3,210	2,794	3,476	14.9	(7.6)	3,112	2,539	3,366	22.6	(7.5)
Others	86	308	291	(72.2)	(70.5)	54	76	55	(28.3)	(1.5)
Total	23,022	21,975	25,079	4.8	(8.2)	13,429	11,735	16,180	14.4	(17.0)
PBIT						PBIT				
Power Systems	1,556	1,395	2,495	11.6	(37.6)	846	809	1,612	4.6	(47.5)
Consumer Products	803	580	671	38.3	19.7	803	580	671	38.3	19.7
Industrial systems	598	526	889	13.6	(32.7)	642	508	780	26.4	(17.7)
Others	16	52	19	(69.2)	(18.0)	10	8	3	26.7	206.5
Total	2,972	2,553	4,074	16.4	(27.0)	2,300	1,905	3,066	20.8	(25.0)
Revenue mix (%)						Revenue mix (%)				
Power Systems	63.3	67.5	67.1			38.0	43.3	51.2		
Consumer Products	23.1	18.8	18.4			39.6	35.2	28.5		
Industrial systems	13.9	12.7	13.9			23.2	21.6	20.8		
Others	0.4	1.4	1.2			0.4	0.6	0.3		
PBIT margins (%)						PBIT margins (%)				
Power Systems	10.7	9.4	14.8			16.6	15.9	19.5		
Consumer Products	15.1	14.1	14.6			15.1	14.1	14.6		
Industrial systems	18.6	18.8	25.6			20.6	20.0	23.2		
Others	18.6	16.7	6.7			17.5	9.9	5.6		
Total	12.9	11.6	16.2			17.1	16.2	18.9		

Source: Company, Kotak Institutional Equities

Full-year estimates imply moderate growth assumptions for remaining 9MFY11E

We have built in a 7.5% yoy consolidated revenue growth for Crompton in FY2011E led by about 17% yoy revenue growth for the standalone entity and a 6.5% revenue de-growth (in Rupee terms) for the subsidiary companies. We expect EBITDA margins to contract slightly, by about 50 bps yoy to 13.5% in FY2011E, from an average of 14% in FY2010. Our assumptions imply a moderate 8.4% yoy revenue growth requirement and relatively flat yoy PAT for the remaining nine months of FY2011E. At the standalone level, our assumptions would imply a revenue growth of 18% for the remaining FY2011E, but expected EBITDA margin contraction leads to a PAT growth requirement of about 10% in remaining 9MFY11E.

Implied numbers for rem. 9MFY11E based on our full-year estimates for the consolidated and standalone entities (Rs mn)

	Consolidated			Standalone		
	Rem 9MFY11E	Rem 9MFY10	% chg.	Rem 9MFY11E	Rem 9MFY10	% chg.
Sales	75,270	69,434	8.4	48,644	41,105	18.3
Expenses	(65,007)	(59,140)	9.9	(41,133)	(34,268)	20.0
Stock	(891)	(540)	64.9	(1,067)	(486)	119.5
Raw material	(46,049)	(41,805)	10.2	(27,073)	(26,890)	0.7
Employee	(9,144)	(8,266)	10.6	(1,512)	(1,928)	(21.6)
Other Exp	(8,924)	(8,529)	4.6	(11,483)	(4,964)	131.3
Operating profit	10,263	10,293	(0.3)	7,511	6,837	9.8
Other income	927	698	32.9	709	603	17.5
EBIDT	11,190	10,991	1.8	8,220	7,441	10.5
Interest	(307)	(220)	39.5	(205)	(49)	314.4
Depreciation	(1,121)	(1,180)	(5.0)	(356)	(391)	(9.0)
PBT	9,762	9,592	1.8	7,659	7,000	9.4
Tax	(3,186)	(2,955)	7.8	(2,578)	(2,378)	8.4
Net profit	6,577	6,636	(0.9)	5,081	4,622	9.9
Key ratios (%)						
Raw material/Sales	62.4	61.0		57.8	66.6	
Employee exp./Sales	12.1	11.9		3.1	4.7	
Other exp./Sales	11.9	12.3		23.6	12.1	
EBITDA margin	13.6	14.8		15.4	16.6	
PBT Margin	13.0	13.8		15.7	17.0	
Tax rate	32.6	30.8		33.7	34.0	
PAT margin	8.7	9.6		10.4	11.2	

Source: Company, Kotak Institutional Equities estimates

Retain estimates; reiterate BUY with a revised target price of Rs290/share

We have retained our EPS estimates of Rs13.2 and Rs15.7 for FY2011E and FY2012E. Our target price of Rs290/share is comprised of (1) 19X Sept-11E earnings of Rs14.4 and (2) Rs10/share for stake in Avantha Power.

We reiterate our BUY rating based on (1) strong domestic business growth potential— contributes to 27% of PBT in FY2010, (2) margin contraction and Europe exposure risks are more contained versus perception, (3) strong cash flow generation characteristics, (4) likely recovery in industrial investments reflected in stronger performance in the industrial systems segment, (5) potential upside from higher participation in substation package tenders, and (6) expected robust T&D spending in XII plan. Our estimates are based on moderate assumptions of (1) about 11% CAGR of revenue and PAT over FY2010E-12E and (2) about 50 bps reduction in margin from FY2010E to FY2012E.

We will revisit our estimate post today's conference call scheduled at 6 pm.

Consolidated financials of Crompton Greaves, March fiscal year-ends, 2006-12E (Rs mn)

	2006	2007	2008	2009	2010	2011E	2012E
Income statement							
Operating income	41,265	56,396	68,323	87,373	91,409	98,292	113,477
Total operating expenses	(38,023)	(51,567)	(60,884)	(77,417)	(78,639)	(85,056)	(98,113)
EBITDA	3,242	4,828	7,439	9,956	12,770	13,236	15,363
Other income	653	1,068	757	587	937	1,110	1,346
Interest expense	(360)	(583)	(781)	(655)	(265)	(357)	(273)
Depreciation	(762)	(954)	(1,263)	(1,216)	(1,551)	(1,536)	(1,624)
Pre-tax profit	2,773	4,360	6,152	8,672	11,891	12,454	14,813
Tax	(453)	(1,495)	(2,054)	(3,047)	(3,650)	(3,980)	(4,729)
Net profits	2,320	2,865	4,098	5,625	8,241	8,474	10,084
EPS (Rs)	8.9	7.8	11.2	15.3	12.8	13.2	15.7
Balance sheet							
Shareholders funds	7,854	9,688	13,018	18,310	25,043	32,147	40,614
Equity share capital	524	733	733	733	1,283	1,283	1,283
Reserves and surplus	7,330	8,955	12,285	17,577	23,760	30,864	39,331
Minority interest	117	284	123	139	43	43	43
Loan funds	4,222	9,045	8,420	7,182	5,010	1,552	552
Secured	3,895	8,726	8,120	6,923	4,766	1,423	423
Unsecured	327	319	300	260	244	130	130
Total sources of funds	12,192	19,017	21,560	25,631	30,095	33,743	41,210
Net block	5,196	9,852	11,968	13,248	12,623	15,076	16,215
Capital work in progress	207	1,021	476	537	1,137	580	580
Net fixed assets	5,403	10,873	12,444	13,785	13,760	15,656	16,795
Investments	651	645	934	1,672	5,536	5,536	5,536
Net current assets (excl. cash)	3,639	4,667	5,149	4,035	4,161	5,392	6,181
Cash	2,073	2,415	2,445	5,656	6,688	7,208	12,747
Net deferred tax asset	426	418	588	482	(49)	(49)	(49)
Total application of funds	12,192	19,017	21,560	25,631	30,095	33,743	41,210
Free cash flow							
Net profit before tax and extraordinary items	2,773	4,360	6,152	8,672	11,891	12,454	14,813
Add: Depreciation / amortisation / non-cash prov	762	954	1,263	1,216	1,551	1,536	1,624
Add: Financial Charges	360	583	781	655	265	357	273
Tax paid	(885)	(1,486)	(2,224)	(2,941)	(3,119)	(3,980)	(4,729)
Operating profit before wcap. changes	3,010	4,410	5,972	7,602	10,588	10,366	11,981
Change in working capital / other adjustments	(1,333)	(1,028)	(481)	1,113	(125)	(1,232)	(789)
Net cashflow from operating activities	1,677	3,382	5,491	8,716	10,462	9,135	11,193
Fixed Assets	(2,618)	(6,424)	(2,834)	(2,557)	(1,526)	(3,432)	(2,764)
Investments	85	6	(290)	(738)	(3,864)	—	—
Cash (used) / realised in investing activities	(2,533)	(6,418)	(3,124)	(3,295)	(5,389)	(3,432)	(2,764)
Free cash flow	(856)	(3,036)	2,367	5,421	5,073	5,703	8,429
Ratios							
EBITDA margin (%)	7.9	8.6	10.9	11.4	14.0	13.5	13.5
Debt/equity	0.5	0.9	0.6	0.4	0.2	0.0	0.0
Net debt/equity	0.3	0.7	0.5	0.1	(0.1)	(0.2)	(0.3)
RoAE (%)	38.5	32.7	35.7	35.7	39.6	29.6	27.7
RoACE (%)	27.0	21.1	22.8	25.7	31.6	27.3	27.4

Source: Company, Kotak Institutional Equities estimates

1QFY11 operating performance largely in line with estimates. JSAW's 1QFY11 revenues of Rs11.4 bn was marginally above our estimate of Rs10.9 bn though EBITDA was 2% lower due to lower volumes but balanced by higher margins per ton (Rs12,160 versus Rs11,600). The management has cautioned on margins trending lower to Rs11,000 per ton due to higher competition (we have factored Rs10,500 per ton). We retain our ADD rating with a price target of Rs256 including value of the investments (Rs70/share) in subsidiaries at 20% holding company discount.

Company data and valuation summary

Jindal Saw

Stock data

52-week range (Rs) (high,low)	227-76
Market Cap. (Rs bn)	59.5

Shareholding pattern (%)

Promoters	46.4
FII's	20.5
MFs	9.6

Price performance (%)

	1M	3M	12M
Absolute	2.2	(5.5)	163.1
Rel. to BSE-30	0.2	(8.3)	116.4

Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	25.0	18.6	17.9
EPS growth (%)	110.8	(25.4)	(4.0)
P/E (X)	8.1	10.8	11.3
Sales (Rs bn)	73.4	59.0	66.7
Net profits (Rs bn)	7.4	5.5	5.3
EBITDA (Rs bn)	13.0	10.7	10.6
EV/EBITDA (X)	5.3	6.0	5.8
ROE (%)	20.5	12.9	11.1
Div. Yield (%)	0.5	0.4	0.4

1QFY11 results—higher-than-expected margin drives in-line operating performance

Jindal SAW reported 1QFY11 PAT of Rs 1.5bn (+11% yoy and -16% qoq) against our estimates of Rs1.68 bn. Revenues at Rs11.4 bn (-24% yoy and +5% qoq) were marginally higher than our estimates at Rs11 bn. EBITDA margin at 22.5% (+660 bps yoy and -400 bps qoq) was lower than our estimate by 100 bps but on a per ton basis (Rs12,160 per ton) it was higher than our estimates (Rs11,600 per ton).

Demand visibility is key for re-rating

Jindal SAW's order book of \$700 mn is down -10% qoq and -10% yoy though it should meet our FY2011E volume estimates of 0.9 mn tons with a few incremental order wins. Along with this, the management has guided for lower per ton margin (Rs11,000 versus Rs12,160 in 1QFY11) for the next 3 quarters of FY2011E on account of rising competition in the Ductile Iron (DI) segment and sluggishness in the oil E&P market.

Maintain ADD with a target price of Rs256

We raise our target price to Rs256 to factor in (1) roll forward in our DCF model and (2) current fair value of investments in group companies. We maintain our ADD rating as the stock is reasonably valued at 10.9X and 6.7X FY2011E EPS and EBITDA, respectively. We would look for (1) traction in order flows for the company and (2) impact of incremental competition on order wins and EBITDA margins in what the company mentioned is a sluggish demand environment.

ADD

JULY 19, 2010

RESULT

Coverage view:

Price (Rs): 202

Target price (Rs): 256

BSE-30: 17,928

QUICK NUMBERS

- PAT up 12% yoy to Rs1.5 bn
- EBITDA margin down 400 bps qoq
- Revenues Rs11.4 bn (4% above KIE estimates)

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In-line results – volumes lower than expected but margins better than expected

JSAW reported 1QFY11 standalone results broadly in line with our estimates with PAT of Rs1.5 bn (estimated Rs1.66 bn) driven by marginally lower-than-expected volumes (around 5% led by seamless and ductile iron) in seamless and ductile iron. EBITDA margins were down 130 bps but up to Rs12,160 per ton (estimated Rs11,600 per ton). Revenues of Rs11.4 bn (estimated Rs10.9 bn) are down 24% yoy and 5% qoq.

1QFY11 operating results have also been affected on account of certain fiscal incentives for the Mundhra facility expiring this quarter which impacted EBITDA by around Rs250mn (9.8% of reported 1QFY11E EBITDA).

Other highlights

- ▶ JSAW's current order book is US\$700 mn (down 10% yoy and qoq) to be executed over FY2011.
- ▶ The management has guided for FY2011E EBITDA margins per ton trending down to Rs11,000 versus Rs12,500 in 1QFY2011 due to rising competition in the DI pipes market and continued sluggishness in the oil E&P market which is leading to higher competition on account of lower capacity utilizations across the industry.
- ▶ MOE (Ministry of Environment) has given in-principle approval for the iron ore mine and the company is expecting to get final approval within the next 2-3 months. Once approved, there would be capital expenditure requirement of Rs1.50 bn for the project.
- ▶ The waterways business is expected to post profits from Sept-2010 quarter onwards.
- ▶ The railways business is currently progressing ahead of expectations with the first wagon expected to roll off the plant by October 1, 2010.
- ▶ The DI pipe segment might come under pressure in the coming quarters as three new players (Tata Metallica, Jai Balaji and Electrotherm) are entering the market with a combined capacity of 0.5 mn ton. The new operators are expected to compete on price to drive utilizations in their new capacities.
- ▶ Standalone (excluding infrastructure-related) capital expenditure would be to the tune of Rs4 bn for the next 15 months.

In-line 1QFY11 results

JSAW, unaudited results (standalone), March year-ends (Rs mn)

	Jun-10	Jun-10E	Jun-09	Mar-10	(% change)		
					KIE est.	yoy	qoq
Net sales	11,350	10,936	15,002	10,863	3.8	(24.3)	4.5
Total expenditure	(8,833)	(8,366)	(12,621)	(7,983)	5.6	(30.0)	10.7
Inc/(Dec) in stock	(1,473)	—	(34)	1,632	—	NM	(190.3)
Raw materials	(5,237)	—	(10,026)	(8,066)	—	(47.8)	(35.1)
Staff cost	(423)	—	(383)	(469)	—	10.4	(9.7)
Outsourcing expense	—	—	(194)	—	—	NA	NA
Other expenditure	(1,700)	—	(1,985)	(1,080)	—	(14.3)	57.3
EBITDA	2,517	2,570	2,381	2,880	(2.1)	5.7	(12.6)
OPM (%)	22.2	23.5	15.9	26.5			
Other income	100	35	14	46	185.7	614.3	117.9
Interest	(276)	(20)	(381)	(218)	1,280.0	(27.6)	26.7
Depreciation	(337)	(345)	(211)	(339)	(2.3)	59.7	(0.6)
Reported pre-tax profits	2,004	2,240	1,803	2,369	(10.5)	11.2	(15.4)
Tax	(493)	(585)	(443)	(566)	(15.7)	11.3	(13.0)
Reported net income	1,511	1,655	1,360	1,803	(8.7)	11.1	(16.2)
Tax rate (%)	24.6	26.1	24.6	23.9			
Volumes (tons)							
Large dia pipes	120,000	120,000	96,400	120,000	—	24.5	—
Ductile iron pipes	61,000	73,000	63,700	73,400	(16.4)	(4.2)	(16.9)
Seamless tubes	26,000	28,000	28,500	28,200	(7.1)	(8.8)	(7.8)

Source: Company, Kotak Institutional Equities estimates

We value JSAW at Rs256/share
JSAW, fair value break-up (Rs/share)

	Rs/share
DCF-value of core business	185
Value of Investments	70
Total value	256
Target Price	256

Source: Kotak Institutional Equities estimates

We value JSAW's investments at Rs70/share
JSAW, value of investments

	Qty (# '000)	Book Value (Rs mn)	Market Price (Rs/share)	Value (Rs mn)
Nalwa sons Investments	268	53	1,025	274
JSL Ltd	4,931	141	106	523
Jindal Steel & Power Ltd (1)	39,449	129	575	22,683
JSW Steel Ltd (1)	1,753	391	1,150	2,016
Shalimar paints Ltd	300	18	407	122
Jindal South West holdings Ltd	95	6	1,793	170
Total		738		25,789
Holding discount @20%				5,158
Net value				20,631
Fully diluted no. of shares (mn)				294.1
Value per share (Rs)				70

Note:

(1) Based on KIE target price

Source: Company, BSE, Kotak Institutional Equities estimates

We value JSAW's core business at Rs185/share

JSAW, DCF based valuation of core business, march fiscal year-ends (Rs mn)

	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	Terminal Value
EBITDA	12,749	9,826	10,453	11,973	12,557	12,819	13,013	12,937	13,080	13,134	
Tax expense	(2,881)	(2,318)	(2,387)	(3,404)	(3,630)	(3,713)	(3,810)	(3,879)	(3,918)	(3,854)	
Changes in working capital	(2,498)	(444)	(1,312)	(2,563)	(1,534)	(578)	(516)	80	(383)	(151)	
Cash flow from operations	7,370	7,064	6,754	6,005	7,392	8,528	8,687	9,137	8,778	9,128	
Capital expenditure	(4,775)	(4,941)	(2,051)	(1,705)	(1,204)	(1,240)	(1,490)	(1,542)	(1,596)	(1,652)	
Free cash flow to the firm	2,595	2,123	4,703	4,300	6,189	7,288	7,197	7,595	7,182	7,476	68,985
Discounted cash flow-now	2,689	1,955	3,851	3,129	4,003	4,191	3,678	3,451	2,900	2,684	
Discounted cash flow-1 year forward		2,200	4,332	3,521	4,504	4,714	4,138	3,882	3,263	3,019	
Discounted cash flow-2 year forward			4,873	3,961	5,066	5,304	4,655	4,367	3,671	3,396	
Discount rate	12.5%										
Growth from 2018 to perpetuity	1.5%										
Discount factor at WACC	1.04	0.92	0.82	0.73	0.65	0.57	0.51	0.45	0.40	0.36	

	+ 1-year	+ 2-years		
Total PV of free cash flow (a)	33,572	55%	35,294	53%
PV of terminal value (b)	27,858	45%	31,340	47%
EV (a) + (b)	61,430		66,634	
Net debt	6,877		6,029	
Equity value	54,553		60,605	
No. of shares	294.1		294.1	
Implied share price (Rs)	185		206	
Exit EV/EBITDA multiple (X)	5.3			
Exit FCF multiple (X)	9.2			

		Sensitivity of share price to WACC and growth rate (Rs)					
		WACC					
		185	11.5%	12.0%	12.5%	13.0%	13.5%
Growth Rate	0.0%	190	181	173	165	158	
	0.5%	195	185	177	169	161	
	1.0%	200	190	181	172	165	
	1.5%	206	195	185	176	168	
	2.0%	213	201	190	181	172	
	2.5%	220	207	196	186	176	
	3.0%	228	214	202	191	181	

Source: Kotak Institutional Equities estimates

Key operating assumptions

Jindal Saw, key operating assumptions (consolidated), December year-ends 2008, March fiscal-year ends, 2010-13E

	2008	2010	2011E	2012E	2013E
Financials					
Revenue	53,558	73,396	58,964	66,694	76,433
EBITDA	7,066	12,749	9,826	10,453	11,973
EBITDA margin (%)	13.2	17.4	16.7	15.7	15.7
Adjusted net profit	3,291	7,436	5,540	5,297	6,317
Diluted EPS	11.9	25.0	18.6	17.9	21.5
Volumes ('000 tons)					
LSAW	344	365	334	360	370
HSAW	135	182	168	193	218
Seamless	68	125	138	150	150
Ductile Iron	234	344	260	300	345
Realisation (\$/ton)					
LSAW	1,667	1,801	1,404	1,419	1,447
HSAW	1,326	888	959	978	998
Seamless	1,429	1,929	1,640	1,672	1,706
Ductile Iron	1,052	1,031	1,031	1,042	1,062
EBITDA					
HSAW (US\$/ton)	161	194	140	140	140
LSAW (US\$/ton)	220	250	225	210	210
Seamless (%)	18.3	23.0	20.0	19.0	19.0
DI (%)	18.0	23.7	23.0	21.0	20.0

Source: Company, Kotak Institutional Equities estimates

Summary financials

Profit model, balance sheet, cash model for Jindal Saw, December year-ends 2007-08, March fiscal year-ends 2010-13E

	2007(1)	2008	2010E (1)	2011E	2012E	2013E
Profit model						
Net revenues	66,957	53,558	73,396	58,964	66,694	76,433
EBITDA	8,371	7,066	12,749	9,826	10,453	11,973
Other income	112	130	286	923	125	125
Interest (expense)/income	(1,684)	(1,979)	(1,842)	(1,325)	(956)	(588)
Depreciation	(773)	(840)	(1,273)	(1,834)	(2,054)	(2,081)
Pretax profits	6,026	4,377	9,918	7,590	7,568	9,428
Tax	(2,777)	(1,087)	(2,433)	(1,973)	(2,119)	(3,204)
Deferred taxation	(63)	(26)	(50)	(76)	(151)	93
Minority interest	56	28	—	—	—	—
Adjusted consolidated net income	5,745	3,291	7,436	5,540	5,297	6,317
Diluted earnings per share (Rs)	21.0	11.9	25.0	18.6	17.9	21.5
Balance sheet						
Total equity	22,750	27,288	36,391	44,227	49,204	55,239
Deferred taxation liability	826	841	890	966	1,117	1,024
Total borrowings	13,455	19,241	14,005	8,279	7,779	5,679
Minority Interest	95	96	96	96	96	96
Current liabilities	10,429	14,573	19,181	14,292	16,211	17,896
Total liabilities and equity	47,555	62,039	70,562	67,861	74,407	79,935
Cash	6,586	5,664	3,710	2,315	5,609	7,229
Other current assets	25,496	32,850	39,868	35,497	38,755	43,040
Total fixed assets	13,380	22,733	26,194	29,259	29,252	28,875
Miscl. Exps. not w/o	—	—	—	—	—	—
Investments	2,093	791	791	791	791	791
Total assets	47,555	62,039	70,562	67,861	74,407	79,935
Free cash flow						
Operating cash flow, excl working capital	14,450	5,145	8,473	6,527	7,378	8,180
Working capital changes	(4,635)	(3,124)	(2,498)	(444)	(1,312)	(2,563)
Capital expenditure	(3,909)	(6,637)	(4,775)	(4,941)	(2,051)	(1,705)
Investments	(718)	783	—	—	—	—
Other income	311	247	286	923	125	125
Free cash flow	5,499	(3,585)	1,487	2,065	4,140	4,037
Ratios (%)						
EBITDA margin (%)	12.5	13.2	17.4	16.7	15.7	15.7
Debt/equity	106.8	39.8	49.4	26.0	18.5	15.6
Net debt/equity	103.9	21.3	42.9	16.9	13.3	4.4
RoAE	15.3	18.6	11.3	20.5	12.9	11.1
RoACE	10.2	17.9	11.3	17.8	12.4	10.7

Note: (1) 15 months period.

Source: Company, Kotak Institutional Equities estimates

JULY 20, 2010
RESULT

Coverage view: **Attractive**

Price (Rs): **570**

Target price (Rs): **550**

BSE-30: **17,928**

Margin decline worrying. 1QFY11 results fell short of our estimates. Revenues fell below our estimate, margins declined more than expected even without absorbing the entire impact of the compensation revision while net income suffered from high tax provisions. The company reiterated its product investment plan of US\$10-11 mn, though this will now spread out rather than concentrated in 1H. We cut our EPS estimate for FY2011E by 16% and maintain our estimates for FY2012E. **REDUCE.**

Company data and valuation summary

Mindtree

Stock data

52-week range (Rs) (high,low) 747-423

Market Cap. (Rs bn) 23.5

Shareholding pattern (%)

Promoters 32.5

FIs 15.8

MFs 11.6

Price performance (%)

Absolute 1M 3M 12M 2.3 (9.8) 16.8

Rel. to BSE-30 0.2 (12.5) (3.9)

Forecasts/Valuations

2010 2011E 2012E

EPS (Rs) 52.2 32.6 51.6

EPS growth (%) 294.3 (37.5) 58.1

P/E (X) 10.9 17.5 11.1

Sales (Rs bn) 13.0 15.6 19.0

Net profits (Rs bn) 2.1 1.3 2.1

EBITDA (Rs bn) 2.5 2.3 3.3

EV/EBITDA (X) 9.4 10.0 6.6

ROE (%) 35.2 19.2 23.7

Div. Yield (%) 0.4 0.6 0.9

Revenues miss estimates; EBITDA margin decline significantly

Mindtree's 1QFY11 was below our estimates on all parameters.

- ▶ Revenues grew 3.4% qoq to US\$77 mn, 2% lower than our expectation. Volumes grew 7.1% sequentially, while pricing declined 3.4% qoq. The company attributes the pricing decline to lower IP/ product compared to the previous quarter. Growth was IT-services driven (+5% qoq).
- ▶ EBITDA margin declined 570 bps sequentially to 12.6%, 70 bps more than our expectation. The management attributed the EBITDA margin decline to wage revision (-370 bps impact), rupee appreciation (-100 bps) and investment in product business (120 bps). The company has absorbed the wage increase for only 77% of the workforce, equivalent to ~80% of the wage bill. Impact of wage revision for the rest will be reflected in 2QFY11.
- ▶ Net income of Rs158 mn (-71% qoq and -72.1% yoy) was 41% lower than our estimate. Net income was impacted by Rs42 mn (ETR of 47% in the quarter) of incremental tax payment on gains from liquidation of a subsidiary.

Operating margin decline concerning

Mindtree reiterated its confidence in maintaining FY2011 operating profit margin in the services business. We are, however, concerned about operating margin performance noting (1) steep 573 bps qoq decline in 1QFY11 that did not include entire impact of wage revision; (2) significant increase attrition rates that moved up to 17.8% on a ttm versus 14.1 in 4QFY10 and (3) lack of any real operating leverage and continued disappointment on the performance front.

Maintain REDUCE rating; cut estimates for FY2011E

We cut our FY2011E EPS estimate by 16% to Rs32.6 and maintain our FY2012E EPS estimate of FY2012. We include US\$10-11 mn of recurring product expenses in our model. We maintain our REDUCE rating noting (1) uncertainty on quantum of investments in the high-risk products business; and (2) continued negative surprises on operating margin performance.

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Update on product business

Mindtree spent US\$1 mn on the products business in 1QFY11. The company indicated that investments in products may spill over to 3QFY11, though the quantum of investments of US\$10-11 mn will remain unchanged. The company expects revenues from products in 2HFY11. The company indicates substantial progress in product development in its wireless infrastructure unit where it is focused on developing IP stacks for LTE and Wimax network infrastructure. Mindtree's focus is on wireless stacks that can deliver business outcome in areas such as bandwidth allocation, ticketing for usage, QoS etc. The company expects some licensing revenues in 2HFY11.

In handsets, the company indicates that its first phone design is completed. Also that product road shows have started with positive initial response from both the US and Europe. Note that Mindtree now plans to launch phone in Europe as well—versus its earlier plan of a US and India focus.

We believe that Mindtree product strategy is high risk on account of:

- ▶ **Limited R&D budgets.** Against the backdrop of heavy R&D budgets of established handset manufacturers, MindTree's budget of US\$10-11 mn appears small. We appreciate that MindTree will not compete directly with established global handset manufacturers, but will face challenge on creating a unique solution.
- ▶ **No prior track record.** We note that a number of international players' diversification into handset business has met with limited success.
- ▶ **Shrinking market for white-labeled smart phones.** We highlight that the market for white-labeled smart phones has reduced after initial success with Windows Mobile OS Smartphone in the early part of the decade. These phones were designed and manufactured by HTC and successfully launched by O2, T-Mobile, AT&T, etc. MindTree believes that it can capture an opportunity available in the white-labeled handset manufacturing space after HTC vacated that space and started competing with handset manufacturers directly.

Exhibit 1: Key changes to estimates, fiscal year-ends March, 2011E-2012E

	New		Old		Change (%)	
	2011E	2012E	2011E	2012E	2011E	2012E
Consolidated						
Revenues (Rs mn)	15,553	18,973	15,360	18,699	1.3	1.5
Revenues (US\$ mn)	338	413	341	413	(0.8)	(0.1)
EBITDA (Rs mn)	2,279	3,316	2,445	3,292	(6.8)	0.7
Net Profit (Rs mn)	1,342	2,122	1,601	2,124	(16.2)	(0.1)
Fully diluted EPS (Rs/share)	32.6	51.6	38.9	51.6	(16.2)	(0.1)
Re/ \$ rate	46.0	46.0	45.0	45.3	2.1	1.6
EBITDA margin (%)	14.7	17.5	15.9	17.6		

Source: Kotak Institutional Equities estimates

Exhibit 2: Mindtree Consulting: Indian GAAP consolidated quarterly earnings statement

Rs mn	Jun-09	Mar-10	Jun-10	qoq (%)	yoy (%)	Kotak E	Deviation
Revenues	3,048	3,444	3,487	1.3	14.4	3,572	(2.4)
Software development expenses	(1,934)	(2,167)	(2,266)	4.6	17.2	(2,436)	(7.0)
Gross profit	1,114	1,277	1,221	(4.3)	9.6	1,136	7.5
SG&A expenses	(607)	(644)	(780)	21.2	28.5	(660)	18.3
EBITDA	507	632	441	(30.3)	(13.0)	476	(7.5)
Depreciation	(161)	(164)	(145)	(11.2)	(9.8)	(164)	(11.5)
EBIT	346	469	296	(37.0)	(14.6)	312	(5.4)
Interest	(24)	(1)	(0)	(83.3)	(99.2)	-	-
Other income	332	197	3	(98.4)	(99.0)	3	2.0
Profit before tax	654	665	299	(55.1)	(54.4)	316	(5.4)
Tax	(87)	(120)	(140)	17	61.6	(47)	
Net profit	567	545	158	(71.0)	(72.1)	268	(41.1)
Minority interest	—	—	—			—	
Share of profit/(loss) in associates	—	—	—			—	
Net income	567	545	158	(71.0)	(72.1)	268	(41.1)
Extraordinaries	—	—	—			—	
Net profit- reported	567	545	158	(71.0)	(72.1)	268	(41.1)
EBITDA margin	16.6	18.4	12.6			13.3	
EPS (Rs/ share)	14.5	13.9	4.0	(71.0)	(72.1)	6.8	(41.1)
Shares outstanding (mn)	39.2	39.2	39.2			39.2	

Source: Company, Kotak Institutional Equities

Exhibit 3: Condensed consolidated financials for MindTree Limited, 2008-2012E, March fiscal year-ends (Rs mn)

	2008	2009	2010	2011E	2012E
Profit model					
Revenues	7,398	12,375	12,960	15,553	18,973
EBITDA	1,254	3,309	2,456	2,279	3,316
Interest (expense)/income	(59)	(162)	(27)	(0)	-
Depreciation	(356)	(570)	(652)	(653)	(779)
Other income	279	(1,974)	770	91	172
Pretax profits	1,118	604	2,547	1,717	2,709
Tax	(85)	(67)	(398)	(375)	(587)
Profit after tax	1,033	537	2,148	1,342	2,122
Diluted earnings per share (Rs)	26.1	13.2	52.2	32.6	51.6
Balance sheet					
Total equity	5,331	5,513	6,706	8,017	9,891
Deferred taxation liability	(90)	(190)	(214)	(214)	(214)
Total borrowings	919	1,394	31	—	—
Minority interest	—	328	—	—	—
Current liabilities	1,392	3,082	2,604	3,087	3,769
Total liabilities and equity	7,553	10,126	9,127	10,890	13,447
Cash	553	488	403	719	1,663
Other current assets	2,765	4,203	4,438	5,388	6,648
Goodwill	214	1,460	154	154	154
Tangible fixed assets	2,625	2,962	2,859	3,357	3,709
Investments	1,395	1,013	1,272	1,272	1,272
Total assets	7,553	10,126	9,127	10,890	13,447
Free cash flow					
Operating cash flow, excl. working capital	1,398	1,889	2,637	2,291	3,316
Tax paid	(188)	(287)	(685)	(375)	(587)
Working capital changes	(408)	251	(713)	(467)	(578)
Capital expenditure	(2,176)	(369)	(473)	(1,162)	(1,131)
Investment changes/acquisition	491	(2,538)	(552)	—	—
Free cash flow	(883)	(1,053)	215	287	1,020
Ratios (%)					
EBITDA margin	16.9	26.7	18.9	14.7	17.5
EBIT margin	12.1	22.1	13.9	10.5	13.4
Debt/equity	0.2	—	—	—	—
Net debt/equity	(0.2)	(0.0)	(0.2)	(0.2)	(0.3)
RoAE	21.3	5.5	35.2	19.2	23.7
RoACE	16.5	32.2	25.8	22.0	28.3

Source: Company, Kotak Institutional Equities

JULY 19, 2010

UPDATE

Coverage view: **Attractive**

Price (Rs): **2,770**

Target price (Rs): **3,100**

BSE-30: **17,986**

Eye on the future. In its annual meeting with analysts, Infosys elaborated on a few themes that underpin its long-term business mix objectives. The themes are aimed at driving non-linearity and negating margin pressures arising out of commoditization of some of the current service offerings. The company also reiterated its positive stance on demand environment, and expressed confidence on curbing attrition rates. We remain positive on Tier-I Indian IT names. Reiterate BUY on Infosys.

Company data and valuation summary

Infosys Technologies

Stock data

52-week range (Rs) (high,low)	2,912-1,870
Market Cap. (Rs bn)	1,590.2

Shareholding pattern (%)

Promoters	16.0
FIs	55.0
MFs	4.0

Price performance (%)

	1M	3M	12M
Absolute	(0.6)	0.7	48.4
Rel. to BSE-30	(2.5)	(2.3)	22.1

Forecasts/Valuations

	2010	2011E	2012E
EPS (Rs)	108.3	124.1	150.0
EPS growth (%)	5.7	14.5	20.9
P/E (X)	25.6	22.3	18.5
Sales (Rs bn)	227.4	276.0	334.0
Net profits (Rs bn)	62.2	71.2	86.1
EBITDA (Rs bn)	78.6	93.4	111.5
EV/EBITDA (X)	18.6	15.3	12.4
ROE (%)	30.1	28.0	28.0
Div. Yield (%)	0.9	1.3	1.5

Preparing for the future – a few key themes

Continuing where it left off in the last analyst meet (where the company had shared its vision of tomorrow's Infosys), Infosys elaborated on a few broad themes it is working on, that will drive its path to achieving the vision. Before getting into the themes, we note that Infosys had indicated a target of 1/3rd revenues each from transformational projects, strategic outsourcing, and new pricing models in its last annual meet. We discuss the four themes the company elaborated on – these are also the central pieces of the company's FY2010 annual report.

- ▶ **Smarter organizations.** Infosys sees itself playing a role in helping its client organizations remodel themselves to be 'smart' and 'agile', as the operating environment becomes challenging and uncertain by the day.
- ▶ **Digital consumers.** Infosys sees this space as one of the next big things with more and more consumer and retail companies trying to tap their consumer base through online channels. Infosys pegged the opportunity size of this market at ~US\$11.2 bn. Infosys is investing in developing solutions and platforms to address this opportunity.
- ▶ **New commerce.** Essentially, new pricing models which de-link revenues from employees – some of the key ones being IP sales, platforms (the company highlighted a few in the healthcare and retail domains), and utility or unit pricing models. Infosys currently derives ~9-10% of its revenues from these models (including Finacle product sales).
- ▶ **Healthcare economy.** Infosys sees tremendous opportunity in this space as (1) Governments and corporations around the world (especially the developed markets) aim to reduce overall healthcare costs, and (2) healthcare payers and providers comply with increasing regulatory oversight. The company indicated a couple of point opportunities thrown by the new healthcare bill in the US – the key one being ICD-9 to ICD-10 transition; Infosys has developed and patented a solution for automated migration to ICD-10 for payers and providers alike. We also note that Infosys has named the head of its Insurance and Healthcare practice, Eric P. as the head of its new public service unit (targeting government projects in developed markets).

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Near term: Reiterates confidence on demand momentum

Infosys management sounded confident on the demand outlook for the Indian IT services industry for FY2011E, while expressing caution on the macro environment, situation in Europe, and the possibility of a double-dip recession. The company believes the worst is behind as far as attrition is concerned and reiterated its view on stable pricing environment. We note that a sharp jump in attrition and drop in offshore pricing had emerged as areas of concern in Infosys' 1QFY11 earnings report, even as the company reported solid 6.9% qoq volume growth.

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

	2008	2009	2010E	2011E	2012E	2013E
Profit model						
Revenues	166,920	216,930	227,420	275,997	334,021	392,703
Cost of sales	(92,070)	(117,650)	(120,710)	(147,701)	(179,710)	(212,052)
SG&A expenses	(22,470)	(27,330)	(28,100)	(34,933)	(42,854)	(51,251)
EBITDA	52,380	71,950	78,610	93,362	111,457	129,399
Depreciation	(5,980)	(7,610)	(9,050)	(9,176)	(10,408)	(12,330)
EBIT	46,400	64,340	69,560	84,186	101,049	117,069
Other income	7,040	4,730	9,430	10,226	12,515	14,065
Pre-tax profits	53,440	69,070	78,990	94,412	113,564	131,134
Provision for tax	(8,060)	(10,270)	(16,810)	(23,196)	(27,459)	(30,877)
Recurring net income	45,380	58,800	62,180	71,217	86,105	100,257
Extraordinaries	1,210	1,080	480	—	—	—
Reported net income	46,590	59,880	62,660	71,217	86,105	100,257
EPS (Rs)	79.1	102.4	108.3	124.1	150.0	174.7
Balance Sheet						
Shareholders funds	137,950	182,540	230,490	278,347	336,366	404,156
Deferred tax liability/(assets)	(1,190)	(1,260)	(2,000)	(2,000)	(2,000)	(2,000)
Borrowings	—	—	—	—	—	—
Minority interest	—	—	—	—	—	—
Total liabilities	136,760	181,280	228,490	276,347	334,366	402,156
Gross block	54,390	70,930	78,390	91,820	108,567	126,395
Accumulated depreciation	(19,860)	(24,160)	(28,930)	(38,106)	(48,514)	(60,844)
Net block	34,530	46,770	49,460	53,714	60,053	65,551
CWIP	13,240	6,770	4,090	4,090	4,090	4,090
Net fixed assets	47,770	53,540	53,550	57,804	64,143	69,641
Cash and bank balances	83,960	112,460	124,480	165,251	212,771	270,499
Net current assets excluding cash	5,030	15,280	50,460	53,292	57,451	62,016
Total assets	136,760	181,280	228,490	276,347	334,366	402,156
Cashflow statement						
Operating profit before working capital changes	52,380	71,950	78,610	93,362	111,457	129,399
Change in working capital/other adjustments	(8,590)	(3,390)	(250)	(2,832)	(4,159)	(4,565)
Capital expenditure	(14,940)	(13,270)	(6,750)	(13,430)	(16,747)	(17,828)
Taxes paid	(6,700)	(9,020)	(17,530)	(23,196)	(27,459)	(30,877)
Free cash flow	22,150	46,270	54,080	53,905	63,091	76,130

Source: Company, Kotak Institutional Equities estimates

June 2010: Earnings announcement calendar

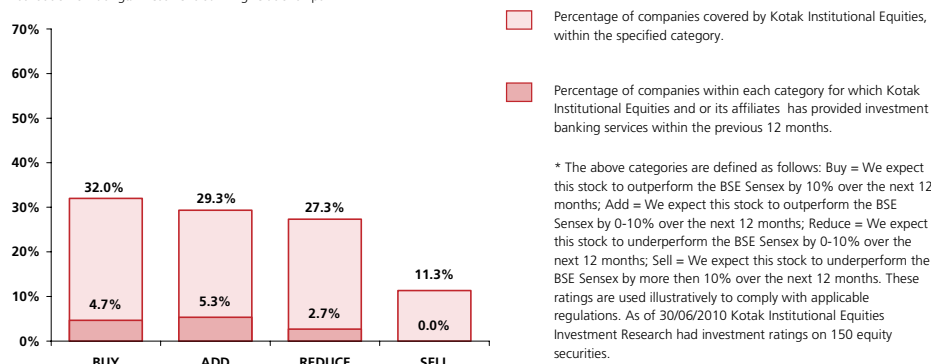
Mon	Tue	Wed	Thu	Fri	Sat
19-Jul	20-Jul	21-Jul	22-Jul	23-Jul	24-Jul
	Bombay Dyeing	Alstom Projects	ACC	Allahabad Bank	Balrampur Chini Mills
	Jindal Hotels	Aries Agro	Ambuja Cements	Areva T&D	Godrej Consumers
	NIIT Tech	Bajaj Finserv	Bajaj Auto	BHEL	Hindustan Zinc
	United Spirits	Birla Corp	Bajaj Holdings & Investments	Biocon	Indiabulls Financial Services
	Zee Entertainment Enterprises	Century Plyboard	Crisil	CESC	Indian Bank
		Engineers India	DishTV	HPCL	IOCL
		Indiabull Power	Dr Reddy Laboratories	IFCI	Jaiprakash Power Ventures
		Kotak Mahindra Bank	Gujarat Gas	Jaiprakash Associates	Maruti Suzuki
		Mastek	IDBI Bank	Jet Airways	
		Rural Electrification Corp	Idea Cellular	Mahindra & Mahindra Financials	
		Thermax	ITC	Praj Industries	
		TVS Motor	Power Finance	UCO Bank	
		United Breweries	Punjab Natiaol Bank	Wipro	
		United Breweries Holdings	Shriram Transport		
		Yes Bank	Thermax		
			Varun Industries		
			Vijaya Bank		
26-Jul	27-Jul	28-Jul	29-Jul	30-Jul	31-Jul
Bharat Forge	Ashok Leyland	Chennai Petroleum	Aban Offshore	ABB	EIH
Century Textiles	Asian Paints	Corporation Bank	Alok Industries	Bharat Electronics	Grasim Industries
Dabur India	Cadila Healthacare	Essel Propack	Bank of Baroda	BPCL	GVK Power & Infra
Essar Oils	Cairn India	Gujarat Mineral Development Corp.	Federal Bank	Hindustan Construction	ICICI Bank
Glaxosmithkline Pharma	Everest Kanto	Havells India	GHCL	Indian Hotels	
Mahindra Holidays	Glenmark Pharmaceuticals	Lupin	GSPL	Max India	
NTPC	Godrej Industries	Mahindra & Mahindra	HCL Technologies	NMDC	
Sterlite Industries	GTL	Phoenix Mills	Hero Honda	PSL	
Tech Mahindra	Hindustan Unilever	Sobha Develpoers	ONGC		
Union Bank	IRB Infrastructure	Sun Pharmaceuticals	Oriental Bank of Commerce		
United Phosporus	JSW Steel	SunTV Network	Petronet LNG		
	Jubilant Organosys	Neyveli Lignite	Siemens		
	L&T	Voltas	Tata Tea		
	Manglore Refinery and Petrochemicals		Ultratech Cement		
	Reliance Industries				
	Titan Industries				
2-Aug	3-Aug	4-Aug	5-Aug	6-Aug	7-Aug
Glaxosmithkline Consumer	Hindalco Industries	IDFC			GMR Infra
India Cements					
Madras Cement					
Nestle India					
9-Aug	10-Aug	11-Aug	12-Aug	13-Aug	14-Aug
	Nagarjuna Constructions		Ranbaxy Laboratories		Lanco Infratech

Source: BSE, Kotak Institutional Equities

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As of June 30, 2010

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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.

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