

**Big brands on summer sale.** We believe the likely reduction in Infosys' FY2008-rupee-based EPS guidance on account of the rupee appreciation is factored in the stock price. Core business drivers including volume, pricing and margins (ex-currency) remain intact and would aptly reflect in Jun' 07 quarter performance. The recent correction in stock prices offers a good entry point. We maintain our attractive view of the sector with Wipro and Infosys as our top picks.

### Valuations—the worst is factored in

We believe the risk-reward ratio has turned favorable for most Indian IT stocks under our coverage after the recent run down in stock prices. The IT sector has underperformed the Sensex by 13.5% and 15% over the past three and six months, respectively. We remain positive on the sector noting that the core business metrics (ex-currency) remain buoyant and that the negatives are already in the price.

### Infosys will likely reduce FY2008 Re EPS guidance, maintain US\$ EPS guidance

We believe Infosys would be able to protect its FY2008 US\$ EPS guidance of 1.86-1.89 by raising US\$ revenue growth guidance to 32-34% (from 28-30%). However, protection of FY2008 EPS growth guidance of 20-22% is unlikely; we expect this number to be revised downwards to 14-16%, implying an EPS of Rs76-78. We expect Satyam to maintain its US\$ EPS guidance and marginally reduce its Re EPS guidance by 1.7% to Rs25.3 from Rs25.7.

### Jun '07 quarter—modest revenue growth, OPM decline

We expect another quarter of strong revenue growth for Tier 1 companies led by volume growth (5-8%) and pricing improvements. We expect Satyam and HCLT to lead the sector in revenue growth (8-9% US\$ terms qoq). Operating margin will likely get impacted by wage hikes, visa costs and rupee appreciation. We expect OPM decline of 250-350 bps for companies that effect wage hikes in the Jun '07 quarter and 50-150 bps for others. Infosys and TCS would be impacted the most as they have effected wage hikes in this quarter.

### Hedging critical for meeting FY2008 expectations

Hedging is critical to meet FY2008 EPS expectations and 1QFY08 EPS guidance. Companies like TCS, Satyam and HCLT with hedges exceeding net monetary assets stand to gain. We expect Satyam to meet its 1QFY08 Re-EPS guidance and Infosys to fall short.

Company	Price (Rs)	Rating	Mkt cap		PER (X)		
	3-Jul-07		(Rs mn)	(US\$ mn)	2007	2008E	2009E
HCL Technologies	335	IL	232,929	5,745	19.1	18.5	15.1
Hexaware Technologies	167	IL	23,764	586	18.8	14.6	11.6
I-flex solutions	2,586	U	215,413	5,313	77.8	50.8	34.9
iGate Global Solutions	307	U	9,718	240	19.6	13.6	10.2
Infosys Technologies	1,947	OP	1,117,607	27,566	29.1	23.2	18.8
Mindtree	773	IL	29,856	736	30.4	25.2	19.3
Mphasis BFL	327	IL	53,578	1,322	44.7	26.1	20.3
Polaris Software Lab	153	U	15,045	371	14.9	12.5	11.3
Satyam Computer Services	471	IL	316,343	7,803	22.0	17.9	14.7
TCS	1,128	IL	1,103,627	27,221	26.7	21.8	17.9
Tech Mahindra	1,427	IL	173,919	4,290	30.4	19.4	13.6
Wipro	515	OP	751,604	18,539	25.4	21.2	16.9

Source: Kotak Institutional Equities estimates.

### INSIDE

[Distressed valuations at Re/US\\$ rate of 40....pg4](#)

[Infosys' likely FY2008 guidance revision....pg6](#)

[Results preview for June 2007 quarter....pg12](#)

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## Table of contents

3	Valuations—the worst is factored in
5	Guidance—maintaining EPS guidance likely to be tough
9	Key considerations for Jun '07 quarter
16	Disclosures

The prices in this report are based on the market close of July 3, 2007.

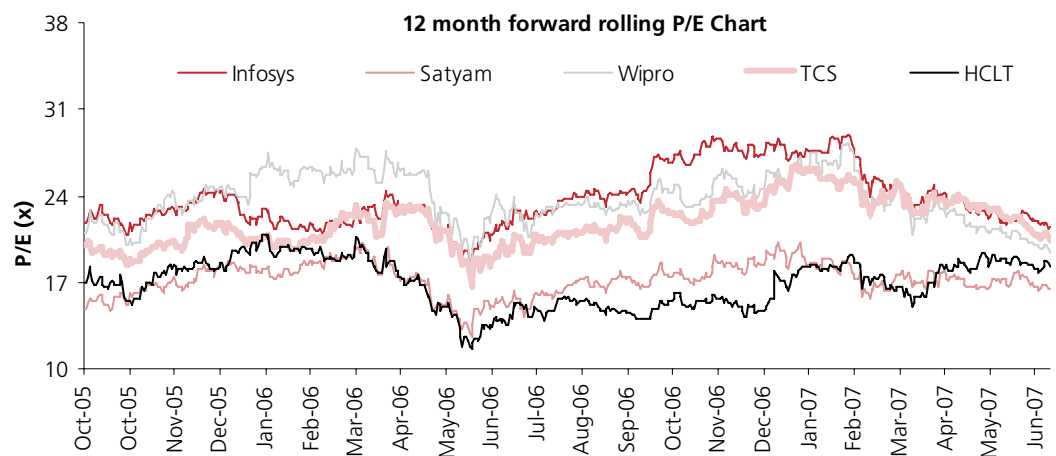
## Valuations—the worst is factored in

We believe the recent decline in IT stocks provides good entry points into some top-tier names. Frontline IT stocks (except HCLT) have corrected between 13% and 19% over the past three months, primarily due to the rupee's appreciation against major currencies (US\$, GBP, and Euro). We believe most of the negatives have been factored into prices. We remain confident on the core business and expect 15%+ returns from tier-I stocks in the next 12 months. Wipro and Infosys are our top picks.

### A time to buy

We believe the risk-reward ratio has turned favorable for most frontline Indian IT stocks. The tier-I companies have underperformed the Sensex by 13-19% and 15-21% over the past three and six months, respectively, and are currently trading at the lower end of their 1-year forward P/E bands (see Exhibit 1). We believe the street has factored in the negative concerns concerning rupee appreciation while overlooking the positives—strong underlying demand and margin protection levers. Despite the appreciating rupee and likely tax rate increase in FY2010, we expect an earnings CAGR of 16-20% for the tier-I companies. We believe that the stocks provide reasonable upsides even assuming a Re/US\$ rate of 40 for FY2008-10. We discuss our distress case valuations of the frontline stocks below. We prefer Infosys and Wipro over other frontline stocks given (a) better growth profile vis-à-vis peers, (b) more operating margin levers like low utilization rates, onsite-offshore mix, performance of subsidiaries/ acquisitions etc, and (c) faster SEZ ramp-up than peers.

Exhibit 1: Frontline IT stocks are trading closer to the lower end of their 12-month forward PE band



Source: Bloomberg, Kotak Institutional Equities estimates.

### Wipro and Infosys provide 7-25% upside even in distress-case scenarios

Exhibit 2 presents our distressed case DCF valuation for the tier-I Indian IT stocks. Our current EPS estimates factor in a Re/US\$ rate of 42, 42, and 41 for FY2008, FY2009, and FY2010, respectively. Assuming a scenario rate of 41 for FY2008 and FY2009, our EPS estimates decline for FY2008 and FY2009 stands at 2-5% for various companies. The target prices in this scenario stand reduced by 2.3-4.3% for various companies. We note that we do not factor in any operational efficiencies or pricing improvements in these scenarios. Wipro and Infosys provide an upside of 17% and 7% over the current levels even at a Re/US\$ scenario rate of 40 for FY2008-FY2010.

Exhibit 2: Infosys and Wipro present reasonable upsides even considering DCF-based fair value at Re/ US\$ rate of 41 and 40

Current assumptions	EPS			EPS CAGR (%)	DCF value (Rs)	Implied P/E (X)			CMP (Rs)	Downside/ upside (%)
	2008E	2009E	2010E			2008	2009	2010		
<b>Re/ US\$ rate</b>	<b>42.0</b>	<b>42.0</b>	<b>41.0</b>							
Infosys	83.8	103.4	110.0	18.0	2,300	27.5	22.2	20.9	1,947	18.1
TCS	51.8	62.9	68.2	17.3	1,300	25.1	20.7	19.1	1,128	15.3
Wipro	24.3	30.4	33.4	18.2	655	26.9	21.5	19.6	515	27.1
Satyam	26.4	32.0	33.5	16.0	510	19.3	15.9	15.2	471	8.2
HCL Technologies	18.1	22.1	23.2	9.7	360	19.8	16.3	15.5	335	7.4
<b>Re/ US\$ rate</b>	<b>41.0</b>	<b>41.0</b>	<b>41.0</b>							
Infosys	80.2	98.9	110.0	18.0	2,200	27.4	22.2	20.0	1,947	13.0
TCS	49.7	60.0	68.2	17.3	1,250	25.1	20.8	18.3	1,128	10.8
Wipro	23.2	28.8	33.4	18.1	640	27.6	22.2	19.2	515	24.2
Satyam	25.7	30.5	33.5	16.0	490	19.1	16.1	14.6	471	3.9
HCL Technologies	17.7	21.7	23.2	9.6	350	19.8	16.1	15.1	335	4.4
<b>Re/ US\$ rate</b>	<b>40.0</b>	<b>40.0</b>	<b>40.0</b>							
Infosys	77.9	94.6	104.7	16.0	2,080	26.7	22.0	19.9	1,947	6.8
TCS	48.0	57.2	64.9	15.4	1,175	24.5	20.6	18.1	1,128	4.2
Wipro	22.3	27.3	31.5	15.9	600	26.9	22.0	19.0	515	16.5
Satyam	24.9	28.9	31.7	14.0	465	18.7	16.1	14.7	471	(1.4)
HCL Technologies	17.2	21.2	22.3	8.3	330	19.1	15.6	14.8	335	(1.5)

Note:

(a) Valuations assuming no changes other than the Re/ USD rate

Source: Kotak Institutional Equities estimates.

## Guidance—maintaining EPS guidance likely to be tough

We expect Infosys to reduce FY2008 Re EPS guidance by 5-7% to Rs76-78. The entire downward revision will likely be on account of rupee appreciation. However, we expect the company to protect its US\$ EPS guidance. Satyam may be better placed than Infosys given its better hedging relative to net monetary assets. We expect Satyam to marginally reduce its Re EPS guidance by 1.7% to Rs25.3 from Rs25.7.

### Maintaining Re EPS guidance for FY2007 unlikely at the current Re/US\$ rate for Infosys

Exhibit 3 depicts our estimates of revenue growth required by Infosys under Re/US\$ scenarios of 41 and 40.7 to maintain EPS guidance. Infosys would need to revise its US\$ revenue growth guidance upwards by 11% (to 41%) to meet its Re EPS guidance at Re/US\$ rate of 40.7. Infosys based its initial FY2008 guidance on Re/US\$ rate of 43.1; likely revised guidance at 40.7 means an appreciation of 5.6% and incremental OPM pressure of 220 bps. We believe that the company would be able to offset 160 bps of pressure on the back of (a) lower variable compensation benefiting the company by 70-80 bps and (b) likely higher pricing from 4QFY07 levels, which was not factored in the guidance by the company. However, 60 bps still remain unaddressed, which in our view will impact the guidance. We expect the eventual Re EPS guidance to be revised down to Rs76-78 based on revenue growth assumption of 32-34% in US\$ terms for FY2008 (see Exhibit 4).

Exhibit 3: Infosys would need 41% (US\$ terms) revenue growth in FY2008 to meet its Re EPS guidance at average Re/US\$ rate of 40.7

Derivation of EPS growth guidance for Infosys for FY2008

	FY2007	FY2008E		FY2008E growth (%)	
		Current	Required	Current	Required
<b>At Re/US\$ rate of 41</b>					
<b>Revenues (US\$ mn)</b>	<b>3,089</b>	<b>4,016</b>	<b>4,289</b>	<b>30</b>	<b>39</b>
Rupee /US\$ rate	45.0	43.1	41.0	(4)	(9)
<b>Revenues (Rs mn)</b>	<b>138,930</b>	<b>173,090</b>	<b>175,865</b>	<b>25</b>	<b>27</b>
EBITDA margin (%)	31.6	31.1	30.5		
EBITDA (Rs mn)	43,910	53,831	53,639	23	22
Depreciation (Rs mn)	(5,140)	(5,600)	(5,700)		
Other income (Rs mn)	3,750	5,000	5,280		
Provision for taxation (Rs mn)	(5,100)	(6,398)	(6,386)		
<b>Net profit (Rs mn)</b>	<b>37,310</b>	<b>46,833</b>	<b>46,833</b>	<b>26</b>	<b>26</b>
Equity shares- weighted average (mn)	555.1	574.0	574.0	3	3
<b>EPS /share (Rs)</b>	<b>67.0</b>	<b>81.6</b>	<b>81.6</b>	<b>22</b>	<b>22</b>
<b>At Re/US\$ rate of 40.7</b>					
<b>Revenues (US\$ mn)</b>	<b>3,089</b>	<b>4,016</b>	<b>4,346</b>	<b>30</b>	<b>41</b>
Rupee /US\$ rate	45.0	43.1	40.7	(4)	(10)
<b>Revenues (Rs mn)</b>	<b>138,930</b>	<b>173,090</b>	<b>176,894</b>	<b>25</b>	<b>27</b>
EBITDA margin (%)	31.6	31.1	30.3		
EBITDA (Rs mn)	43,910	53,831	53,599	23	22
Depreciation (Rs mn)	(5,140)	(5,600)	(5,700)		
Other income (Rs mn)	3,750	5,000	5,320		
Provision for taxation (Rs mn)	(5,100)	(6,398)	(6,386)		
<b>Net profit (Rs mn)</b>	<b>37,310</b>	<b>46,833</b>	<b>46,833</b>	<b>26</b>	<b>26</b>
Equity shares- weighted average (mn)	555.1	574.0	574.0	3	3
<b>EPS /share (Rs)</b>	<b>67.0</b>	<b>81.6</b>	<b>81.6</b>	<b>22</b>	<b>22</b>

Source: Kotak Institutional Equities estimates.

Exhibit 4: Infosys's likely Re EPS guidance would be Rs76-78 for FY2008  
Derivation of likely revised FY2008 EPS guidance of Infosys

	FY2007	FY2008E (a)		FY2008E growth (%)	
		Lower end	Upper end	Lower end	Upper end
<b>At Re/US\$ rate of 40.7</b>					
<b>Revenues (US\$ mn)</b>	<b>3,089</b>	<b>4,077</b>	<b>4,139</b>	<b>32</b>	<b>34</b>
Rupee /US\$ rate	45.0	40.7	40.7	(10)	(10)
<b>Revenues (Rs mn)</b>	<b>138,930</b>	<b>165,953</b>	<b>168,468</b>	<b>19</b>	<b>21</b>
EBITDA margin (%)	31.6	29.8	30.3		
EBITDA (Rs mn)	43,910	49,454	51,046	13	16
Depreciation (Rs mn)	(5,140)	(5,600)	(5,700)		
Other income (Rs mn)	3,750	5,280	5,320		
Provision for taxation (Rs mn)	(5,100)	(5,405)	(6,080)		
<b>Net profit (Rs mn)</b>	<b>37,310</b>	<b>43,729</b>	<b>44,586</b>	<b>17</b>	<b>20</b>
Equity shares- weighted average (mn)	555.1	574.0	574.0	3	3
<b>EPS /share (Rs)</b>	<b>67.0</b>	<b>76.2</b>	<b>77.7</b>	<b>14</b>	<b>16</b>

Source: Kotak Institutional Equities estimates.

### US\$ EPS guidance may be protected

We believe that Infosys may be able to protect the upper end of its FY2008 EPS guidance of US\$1.89. Based on our calculations, the company needs to increase revenue guidance to 34% at the upper end of the band assuming that the guidance for the remainder of the year is based on Re/US\$ rate of Rs40.7 (see Exhibit 5). Exhibit 6 details the revision in US\$ revenue growth guidance by Infosys in after past June quarter results.

Exhibit 5: Infosys will likely maintain US\$ EPS guidance for FY2008  
Derivation of likely FY2008 EPS guidance of Infosys

	FY2007	FY2008E (a)		FY2008E growth (%)	
		Lower end	Upper end	Lower end	Upper end
<b>At Re/US\$ rate of 40.7</b>					
<b>Revenues (US\$ mn)</b>	<b>3,089</b>	<b>4,077</b>	<b>4,145</b>	<b>32</b>	<b>34</b>
EBIT margin (%)	27.6	26.4	26.8		
EBIT (US\$ mn)	852	1,076	1,111	26	30
Other income	84	122	122		
Provision for taxation	(112)	(132)	(148)		
<b>Net profit (US\$ mn)</b>	<b>822</b>	<b>1,067</b>	<b>1,085</b>	<b>30</b>	<b>32</b>
Equity shares- weighted average (mn)	555.1	574.0	574.0	3	3
<b>EPS /share (US\$)</b>	<b>1.48</b>	<b>1.86</b>	<b>1.89</b>	<b>26</b>	<b>28</b>

Source: Kotak Institutional Equities estimates.

Exhibit 6: Infosys has raised its US\$-revenue guidance by 0.6-8.7% after 1Q over the past four fiscals  
Infosys' guidance revision history

	Guidance				Actual	Guidance initial (%)	Deviation from initial guidance (% pts)		
	Initial	End of 1Q	End of 2Q	End of 3Q			After 1Q	After 2Q	After 3Q
<b>FY2007</b>									
Revenues (US\$ mn)	2,800	2,920	3,040	3,090	3,092	30.2	5.6	11.2	13.5
Revenues (Rs bn)	124.5	134.0	139.0	139.2	138.9	30.7	10.0	15.3	15.5
EPS (Rs)	57.8	62.9	66.0	66.6	66.9	28.4	11.2	18.2	19.6
<b>FY2006</b>									
Revenues (US\$ mn)	2,070	2,080	2,140	2,140	2,150	30.0	0.6	4.4	4.4
Revenues (Rs bn)	90.3	90.5	93.8	95.0	95.2	26.6	0.3	5.0	6.5
EPS (Rs)	43.0	43.0	44.7	45.2	45.0	21.9	0.1	5.0	6.2
<b>FY2005</b>									
Revenues (US\$ mn)	1,392	1,485	1,561	1,591	1,592	31.0	8.7	15.9	18.7
Revenues (Rs bn)	60.4	67.7	71.6	71.1	71.3	26.9	15.4	23.5	22.4
EPS (Rs)	28.0	31.4	33.5	34.4	35.2	19.5	14.3	23.5	27.1
<b>FY2004</b>									
Revenues (US\$ mn)	963	982	1,015	1,053	1,063	27.8	2.5	6.9	11.9
Revenues (Rs bn)	45.7	45.7	46.6	47.2	47.6	26.0	0.1	2.6	4.3
EPS (Rs)	20.5	21.2	22.4	23.3	23.4	13.4	4.0	10.6	15.7

Source: Company reports, Kotak Institutional Equities.

## Operating margin reconciliation—levers available at the disposal

Exhibit 7 depicts the levers which Infosys may be able to utilize to offset the impact of varying pressures including visa costs, wage revisions and rupee appreciation. Infosys has total levers of ~900 bps, of which it can pull 575 bps in FY2008, in our view. Assuming that FY2008 EPS guidance is based on 40.7, we forecast OPM decline of 130-180 bps in FY2008.

Exhibit 7: Infosys has several margin levers to limit the impact of rupee appreciation on margins  
Derivation of Infosys' FY2008 EBITDA margins at Re/US\$ rate of 40.7

FY2007 EBITDA margin (%)		31.6		Currency impact computation	
Negatives (bps)		(708)		Avg Re/US\$ rate FY2007	45.1
Positives (bps)		575		Avg Re/US\$ rate FY2008E	40.7
Net impact (bps) (a)		(133)		Appreciation (%)	(9.7)
<b>FY2008E EBITDA margin (%)</b>		<b>30.3</b>		Per % impact (bps)	40
				<b>Total impact (bps)</b>	<b>(388)</b>
<b>Negatives</b>					
					<b>Margin impact</b>
Wage inflation onsite					(120)
Wage inflation offshore					(200)
Rupee appreciation (a)					(388)
<b>Total negative</b>					<b>(708)</b>
<b>Positives</b>					
<b>Buffer</b>	<b>FY2007</b>	<b>Best case scenario</b>	<b>Total buffer available</b>	<b>FY2008E</b>	<b>Margin impact</b>
Utilization rate (%) (b)	68.0	75	210	72	120
Pricing improvement (%) (blended)	4.6	4-5	150	4	190
Profitability of subsidiaries			100	50	50
SG&A leverage			120	60	60
Employee pyramid (c)	57.0	60	100	58	35
Onsite offshore mix (d)	48.0	50	80	49	40
Variable costs			150	80	80
<b>Total positive</b>			<b>910</b>		<b>575</b>
<b>Net impact in FY2008</b>					<b>(133)</b>

Note:

- (a) At Re/US\$ assumption of 40.7 FY2007 average rate realized was 45.
- (b) Net utilization rate excluding support but including trainees
- (c) Denotes the # of employees in the 0-3 years experience band
- (d) % revenues offshore

Source: Kotak Institutional Equities estimates.

## Satyam—better placed than peers

We expect Satyam to maintain its US\$ EPS guidance and marginally reduce its Re EPS guidance by 1.7% to Rs25.3 from Rs25.7. Satyam gets an additional benefit of Rs400 mn of likely profits from forward hedges in excess of net monetary assets. We believe the company will likely raise its FY2008 US\$ revenue growth guidance by 4% to a growth of 32-34%. Exhibit 8 details our likely EPS assumptions scenario for FY2008 and Exhibit 9 details the revision in US\$ revenue growth guidance by Satyam after past June quarter results.

Exhibit 8: Satyam will likely reduce its Re EPS guidance for FY2008 marginally

At Re/US\$ rate of 40.7	FY2007	FY2008E (a)		FY2008E growth (%)	
		Lower end	Upper end	Lower end	Upper end
<b>Revenues (US\$ mn)</b>	<b>1,439</b>	<b>1,904</b>	<b>1,932</b>	<b>32</b>	<b>34</b>
Rupee /US\$ rate	45.1	40.7	40.7	(10)	(10)
<b>Revenues (Rs mn)</b>	<b>64,851</b>	<b>77,502</b>	<b>78,644</b>	<b>20</b>	<b>21</b>
EBITDA margin (%)	23.7	22.9	22.9		
EBITDA (Rs mn)	15,377	17,748	18,010	15	17
Depreciation (Rs mn)	(1,484)	(1,670)	(1,670)		
Other income (Rs mn)	1,674	2,950	2,950		
Provision for taxation (Rs mn)	(1,520)	(2,283)	(2,315)		
<b>Net profit (Rs mn)</b>	<b>14,047</b>	<b>16,745</b>	<b>16,975</b>	<b>19</b>	<b>21</b>
Equity shares- weighted average (mn)	655.0	671.0	671.0	2	2
<b>EPS /share (Rs)</b>	<b>21.4</b>	<b>25.0</b>	<b>25.3</b>	<b>16</b>	<b>18</b>

Source: Kotak Institutional Equities estimates.

Exhibit 9: Satyam has raised its US\$-revenue guidance by 1.2-3.2% after 1Q over the past three fiscals  
Satyam's guidance revision history

	Guidance				Actual	Guidance initial (%)	Deviation from initial guidance (% pts)		
	Initial	End of 1Q	End of 2Q	End of 3Q			After 1Q	After 2Q	After 3Q
<b>FY2007</b>									
Revenues (US\$ mn)	1,381	1,395	1,440	1,445	1,460	26.0	<b>1.3</b>	5.4	5.8
Revenues (Rs bn)	61.0	62.9	64.8	64.4	64.9	27.3	4.0	7.8	7.1
EPS (Rs)	18.3	19.8	20.8	20.9	21.5	20.0	9.5	16.5	17.0
<b>FY2006</b>									
Revenues (US\$ mn)	1,034	1,059	1,088	1,094	1,096	30.3	<b>3.2</b>	6.8	7.6
Revenues (Rs bn)	45.0	45.7	47.2	47.9	47.9	30.0	1.9	6.2	8.2
EPS (Rs)	13.7	13.7	14.6	15.2	15.3	15.6	0.6	8.2	13.0
<b>FY2005</b>									
Revenues (US\$ mn)	736	743	770	785	794	30.0	<b>1.2</b>	6.0	8.5
Revenues (Rs bn)	31.5	33.1	34.3	34.3	34.6	23.8	6.5	11.1	11.3
EPS (Rs)	10.3	11.0	11.4	11.5	11.8	16.9	8.2	12.1	13.5

Source: Company reports, Kotak Institutional Equities.



## Key considerations for Jun '07 quarter

We believe the sharp rupee appreciation during the quarter may lead to Indian IT companies missing their revenue and EPS guidance for the quarter in Re terms despite strong qoq revenue growth in US\$ terms. We expect 4-14% and 2-11% US\$ revenue growth for tier-I and tier-II companies. We forecast a qoq OPM decline of 50-260 bps for the tier-I names in our coverage universe as a result of rupee appreciation, wage revisions, and higher visa costs. Net income impact would be mitigated to some extent by gains on forex hedges.

### Expect revenue guidance outperformance in US\$ terms, shortfall in Re terms

Frontline IT companies have proffered qoq revenue growth guidance of 3-5.5% (US\$ terms) for the Jun '07 quarter (see Exhibit 10). We expect most of the companies to outperform their US\$-based guidance by 0.9-3.2% (see Exhibit 11). However, the rupee's appreciation against the US\$, GBP, and Euro may lead to the companies missing their Re-based revenue and EPS guidance by 1-3%. Among the frontline companies, we expect Satyam and HCLT to lead the qoq revenue growth rates with 8-9% qoq revenue growth rate (US\$-terms).

Exhibit 10: Revenue and EPS guidance for various Indian IT companies for Jun '07 quarter

	Actuals	Guidance		
	4QFY07	1QFY08	qoq (%)	yoy (%)
<b>Infosys</b>				
Revenues (US\$ mn)	863.0	908.0	5.2	37.6
Revenues (Rs bn)	37.7	39.1	3.7	29.8
EPS (Rs)	18.1	17.8	(1.4)	24.2
EPADS (US\$)	0.4	0.4	—	28.2
Re/US\$ rate	43.8	43.1		
<b>Wipro</b>				
Revenues (US\$ mn)	690.7	711.0	2.9	31.8
<b>Satyam</b>				
Revenues (US\$ mn)	411.3	434.0	5.5	34.6
Revenues (Rs bn)	17.8	18.1	1.7	25.4
EPS (Rs)	6.0	6.0	—	10.0
EPADS (US\$)	0.3	0.3	3.8	14.9
Re/US\$ rate	43.9	42.3		
<b>Patni</b>				
Revenues (US\$ mn)	156.0	163.0	4.5	25.5
Net income (US\$ mn)	27.8	23.0	(17.3)	59.3
<b>Hexaware</b>				
Revenues (US\$ mn)	60.1	65.0	8.1	43.8
Net income (US\$ mn)	8.0	7.2	(10.2)	10.8
Re/US\$ rate	44.0	42.0		

Source: Companies, Kotak Institutional Equities.

Exhibit 11: We expect Infosys, Wipro, and Satyam to outperform their 1QFY08 revenue guidance by 0.9-2.3%  
Guidance and actual revenues, 1QFY06-1QFY08E

	1QFY06	2QFY06	3QFY06	4QFY06	1QFY07	2QFY07	3QFY07	4QFY07	1QFY08E
<b>Wipro</b>									
<b>Revenues (US\$ mn)</b>									
Guidance	395	422	463	510	533	577	633	685	711
Actual (a)	399	431	473	512	539	589	641	691	717
<b>Growth qoq (%)</b>									
Guidance	5.4	5.9	7.5	7.7	4.0	7.0	7.5	6.9	2.9
Actual (a)	6.4	8.1	9.9	8.2	5.3	9.2	8.8	7.8	3.9
<b>Outperformance (% pts)</b>	<b>0.9</b>	<b>2.2</b>	<b>2.4</b>	<b>0.5</b>	<b>1.2</b>	<b>2.2</b>	<b>1.3</b>	<b>0.9</b>	<b>0.9</b>
<b>Infosys</b>									
<b>Revenues (US\$ mn)</b>									
Guidance	463	509	558	584	633	715	795	861	908
Actual (a)	476	524	559	593	660	746	821	862	924
<b>Growth qoq (%)</b>									
Guidance	1.6	7.0	6.4	4.5	6.7	8.3	6.6	4.9	5.2
Actual (a)	4.4	10.2	6.6	6.2	11.3	12.9	10.1	5.0	7.2
<b>Outperformance (% pts)</b>	<b>2.8</b>	<b>3.2</b>	<b>0.2</b>	<b>1.7</b>	<b>4.6</b>	<b>4.6</b>	<b>3.5</b>	<b>0.1</b>	<b>2.0</b>
<b>Satyam</b>									
<b>Revenues (US\$ mn)</b>									
Guidance	236	259	280	299	310	339	373	395	434
Actual (a)	246	268	282	301	323	352	376	411	447
<b>Growth qoq (%)</b>									
Guidance	4.9	5.2	4.5	6.0	3.1	5.0	6.1	5.1	5.6
Actual (a)	9.4	8.9	5.2	6.7	7.2	9.1	6.7	9.4	8.8
<b>Outperformance (% pts)</b>	<b>4.5</b>	<b>3.6</b>	<b>0.7</b>	<b>0.7</b>	<b>4.2</b>	<b>4.2</b>	<b>0.6</b>	<b>4.3</b>	<b>3.2</b>

Note:

(a) Kotak estimates for 1QFY08

(b) Guidance and actual revenues for Wipro's Global IT (IT services + BPO) business only

(c) Wipro's guidance and actuals for 1QFY07 and 2QFY07 factor in acquisitions

(d) Consolidated US GAAP guidance and actuals for Satyam

Source: Company, Kotak Institutional Equities estimates.

### OPM decline likely to be severe

We forecast qoq OPM decline for all the companies under our coverage universe. The extent of the operating margin decline is contingent on (a) wage increase cycle: Infosys effects wage increases for all the employees in the June quarter. TCS also effects wage increases for all employees in the June quarter but leaves promotions to the subsequent quarter. Satyam has a wage increase cycle in the September quarter; and (b) dependency on H1B visas: An H1B visa costs US\$3,000-3,500 per application to process. Infosys relies almost exclusively on H1B visas; Satyam and Wipro has high exposure to H1Bs. TCS has the least dependence. Overall, we expect a 2.6% OPM decline for Infosys, 2.6% for TCS, 1.3% for Wipro (Global IT) and 0.8% for Satyam.

### Forex hedges may partly mitigate impact of rupee appreciation at the net income level

Net income impact would be mitigated to some extent by gains on forex hedges. We expect HCL Tech (Rs1.2 bn) and TCS (Rs800 mn) to report the highest forex gains among the tier-I names given their large hedging positions at end-Mar 2007 (see Exhibit 12).

Exhibit 12: Currency hedges of Indian IT companies as on March 31, 2007

mn	US\$	Euro	Pound Sterling	Total (a)	Remarks
Infosys (b)	377	26	30	471	
Wipro	600			600	Between 44 and 45.77
Satyam	453			453	
TCS	1,135	107	78	1,431	
HCL Tech	900			900	
Patni	193			193	Between 43.86 and 46.85
Hexaware	60			60	

Note:

(a) Computed at cross-currency rates as on Mar 31, 2007

(b) Infosys and Satyam currently have hedges of US\$600 mn and US\$650 mn respectively

Source: Companies, Kotak Institutional Equities.

Exhibit 13 provides our forecasts for the Jun '07 quarter for the companies in our coverage universe.

Exhibit 13: Results preview for the quarter ending June 2007 (Rs mn)

Key financials	Jun-06	Mar-07	Jun-07	%qoq	%yoy	Comments/What to look for
<b>TCS: Results (July 16)</b>						
Revenues	41,443	51,464	51,456	(0.0)	24.2	• We expect revenue growth of 7.2% in US\$ terms driven by volume growth of 8.3%.
Operating profit	10,169	14,608	13,255	(9.3)	30.4	• OPM will likely decline 260bps qoq as a result of (a) sharp rupee appreciation and (b) wage revisions during the quarter
Adjusted net profit	8,626	11,728	11,146	(5.0)	29.2	• Our forecast factors in a forex gain of Rs800 mn. TCS had forex gains of Rs 578 mn in the Mar'07 quarter and had hedges of US\$1.4 bn as on Mar 31, 2007
Operating profit margin (%)	24.5	28.4	25.8	—	—	• Expect investor focus on commentary on (a) margins for FY2008 and (b) likely overall revenue growth outlook for FY2008
<b>Wipro: Results (July 3<sup>rd</sup> week)</b>						
Total revenues	31,312	43,345	40,985	(5.4)	30.9	• We expect 3.9% qoq revenue growth for Global IT services business (in US\$ terms), 1% higher than company's guidance of US\$711 mn
Global IT revenues	24,513	30,357	29,412	(3.1)	20.0	• We expect Global IT OPM to decline 130bps on account of rupee appreciation during the quarter; Wipro had hedges of US\$600 mn as on Mar 31, 2007
Operating profit	6,509	8,187	7,638	(6.7)	17.3	• We expect a strong 2QFY08 guidance from Wipro; Sep and Dec have typically been the strongest quarters for Wipro
Adj. net profit	6,038	7,874	7,117	(9.6)	17.9	• Expect investor focus on (a) performance in telecom vertical, specially in telecom OEM segment (b) sustainability of BPO revenue growth
Total Operating profit margin (%)	20.8	18.9	18.6	—	—	• Expect investor focus on the impact on margin from potential change in wage increase cycle to September quarter vs. December quarter earlier
Global IT - OPM (%) (b)	24.3	23.7	22.4	—	—	• June is a seasonally weak quarter for Wipro Infotech business—hence qoq decline in overall revenues
<b>Infosys Technologies: Results (July 11)</b>						
Revenues	30,150	37,720	37,847	0.3	25.5	• We expect 7.2% qoq revenue growth in 1QFY08 (US\$ terms) to US\$924 mn, 2% higher than company's guidance of 5.2% qoq growth
Operating profit	8,890	11,970	11,031	(7.8)	24.1	• We expect Infosys to miss its 1QFY08 EPS guidance of Rs17.84; we forecast an EPS of Rs17.4, 2.3% lower than the company's guidance
Adjusted net profit	8,080	10,200	10,014	(1.8)	23.9	• Our numbers factor in a forex gain of Rs280 mn against a forex loss of Rs50 mn in the previous quarter; Infosys increased its hedges to US\$600 mn during the quarter
Operating profit margin (%)	29.5	31.7	29.1	—	—	• Expect investor focus on (a) guidance revisions--we expect an increase in \$ term revenue guidance (b) We expect downward revision in FY2008 rupee EPS guidance but US\$ EPS guidance to be maintained
<b>Satyam Computer Services: Results (July 20)</b>						
Revenues	14,429	17,792	18,070	1.6	25.2	• We expect Satyam to lead the industry in revenue growth in the Jun '07 quarter. We expect 8.7% revenue growth (US\$ terms), 3.2% higher than company's guidance
Operating profit	3,550	4,102	4,029	(1.8)	13.5	• Expect OPM to decline 80bps as a result of (a) rupee appreciation and (b) visa costs. We factor in forex gains of RS400 mn as against Rs33 mn in the last quarter.
Adjusted net profit	3,541	3,936	4,011	1.3	13.3	• Expect investor focus on (a) guidance revision--we expect Satyam to raise its US\$ revenue guidance and marginally reduce its EPS guidance for the year and (b) commentary on pricing improvements
Operating profit margin (%)	24.6	23.1	22.3	—	—	• 1QFY08 revenue guidance stands at Rs18.01-18.1bn, implying 1.2-1.7% qoq growth. EPS guidance stands flat at Rs5.98. Satyam's guidance is based on a Re/US\$ rate of 42.3
<b>HCL Technologies: Results (August 2<sup>nd</sup> week)</b>						
Revenues	12,538	15,767	16,150	2.4	28.8	• Expect revenue growth of 8.7% in US\$ terms led by (a) continued momentum in infrastructure services (b) large deal ramp up in IT services. Expect BPO to consolidate after the 18% growth in the Mar '07 qtr
Operating profit	2,727	3,473	3,470	(0.1)	27.2	• OPM expected to decline 50bps as a result of rupee appreciation and higher visa costs
Adjusted net profit	2,242	3,120	3,921	25.7	74.9	• We factor in forex gains of Rs1.2 bn for HCLT during the quarter. Note that HCLT had forex hedges of US\$900 mn as on Mar 31, 2007, much higher than its net monetary exposure
Operating profit margin (%)	21.8	22.0	21.5	—	—	• Our estimates and previous quarter numbers factor in charge related to issue of stock options at discount to the market price
<b>Tech Mahindra: Results (July 19)</b>						
Revenues	5,871	8,745	9,304	6.4	58.5	• Expect pace of growth in BT account to reduce somewhat (12% vs. 19.3% in the previous quarter) after phenomenal growth in the previous year
Operating profit	1,308	2,218	2,054	(7.4)	57.0	• We forecast 14.5% qoq revenue growth (US\$-terms) to be driven by non-BT accounts and ramp up in BPO business
Adjusted net profit	1,066	1,960	1,692	(13.7)	58.7	• Expect OPM decline of 330bps on account of (a) rupee appreciation (b) wage hikes (c) visa costs and (d) investments in BTGS deal and BPO
Operating profit margin (%)	22.3	25.4	22.1	—	—	• Expect investor focus on (a) progress on BTGS deal (b) traction in non-BT, non-AT&T accounts

Source: Kotak Institutional Equities estimates.

## Results preview for the quarter ending June 2007 (Rs mn)

Key financials	Jun-06	Mar-07	Jun-07	%qoq	%yoy	Comments/What to look for
<b>i-flex solutions: Results (July 4<sup>th</sup> week)</b>						
Revenues	4,075	5,794	5,770	(0.4)	41.6	• We expect new license signings to be US\$22.2 mn (US\$25.2 mn in the previous quarter). For FY2008 we expect new license signings of US\$110 mn
Products revenues	2,000	3,206	3,203	(0.1)	60.2	• We expect license fees recognition to grow 14% qoq to Rs801 mn from Rs705 mn in 4QFY07
Services revenues	1,984	2,445	2,416	(1.2)	21.8	• We expect services revenue growth to moderate (expect 4% qoq growth) after the strong growth in the previous quarter
Operating profit	458	1,093	1,019	(7)	122.4	• Expect investor interest to be restricted to the possibility of further open offer by Oracle and stock's delisting. Oracle now owns 82.1% of the company
Adjusted net profit	415	777	687	(11.5)	65.8	
Operating profit margin (%)	24.0	18.9	17.7	—	—	
<b>MindTree Consulting: Results (July 24)</b>						
Revenues	1,333	1,566	1,614	3.1	21.1	• We expect a 10.8% qoq increase in revenues driven by strong volume growth of 9.7% and pricing improvement of 1%
Operating profit	273	289	289	(0.3)	5.7	• Rupee appreciation (7% during the quarter) to impact Re terms revenue growth. We expect 3.1% revenue growth qoq in Re terms
Adjusted net profit	238	246	237	(3.6)	(0.1)	• OPM likely to decline 60bps qoq as a result of (a) rupee appreciation (b) wage hikes--MT effects wage hikes at junior levels this quarter and (c) visa costs
Operating profit margin (%)	20.5	18.5	17.9	—	—	• Net income expected to decline 3.6% in Re terms. MT has US\$13mn of forex hedges earmarked for this quarter with net receivable at US\$35mn. We do not expect significant forex gains
<b>Mphasis BFL: Results (July 4<sup>th</sup> week)</b>						
Revenues	2,607	3,372	3,421	1.4	31.2	• We expect another quarter of strong revenue growth led by revenues from EDS and EDS clients
IT Services	1,828	2,291	2,323	1.4	27.1	• Revenue growth primarily on the back of growth in IT services business
Msource	779	1,081	1,098	1.5	40.9	• Expect OPM decline of 400bps on accounts of rupee appreciation, wage revisions, and ongoing investments in systems and infrastructure
Operating Profit	315	646	521	(19.5)	65.4	• Expect investor focus on potential ramp up from some of the large deals bagged by EDS
Adjusted net Profit	152	456	341	(25.1)	124.6	• Expect investor focus on commentary on (a) ramp up in various channels of EDS revenues (b) headcount and revenue targets of the combined entity
Operating profit margin (%)	12.1	19.2	15.2	—	—	
<b>Polaris Software Lab: Results (July 4<sup>th</sup> week)</b>						
Revenues	2,320	2,708	2,681	(1.0)	15.5	• Sustainability of revenue growth rates remains the key to stock performance
Operating profit	360	322	298	(7.5)	(17.3)	• Client acquisition pace and account mining remain the key; success of Intellect as an entry point to win clients needs to be validated
Adjusted net profit	203	214	179	(16.5)	(11.8)	• Operating margins to decline marginally led by a) rupee appreciation and b) visa costs
Operating profit margin (%)	5.8	11.9	11.1	—	—	• Expect investor focus on steps being taken to improve client mining (the company now has 18 AAA accounts) and drive operational efficiencies
<b>Hexaware Technologies: Results (July 3<sup>rd</sup> week)</b>						
Revenues	2,069	2,644	2,673	1.1	29.2	• We expect revenue growth of 8.5% in US\$ terms and 1.1% in rupee terms
Operating profit	311	395	330	(16.5)	6.2	• We expect OPM to decline 270bps qoq as a result of (a) wage inflation (b) rupee appreciation and (c) higher visa costs. The company has factored in a 250bps decline in its net income guidance
Adjusted net profit	298	352	295	(16.2)	(0.9)	• Expect investor focus on commentary on a) sales execution improvement initiative and b) impact of ramp down on select accounts on organic growth
Operating profit margin (%)	15.0	15.0	12.3	—	—	• Hexaware has given a revenue growth guidance of 6.5-8.1% to US\$64-65mn and a net income guidance of US\$7-7.2 mn, implying a sequential decline of 10.2-12.7%
<b>iGate Global Solutions: Results (July 11)</b>						
Revenues	1,816	2,101	2,017	(4.0)	11.1	• We expect nominal US\$ terms qoq revenue growth of 2-3% driven by ramp-down in sub-prime mortgage accounts.
Operating profit	129	322	232	(27.9)	79.8	• We expect OPM to decline 380bps qoq as a result of rupee appreciation and wage hikes effected during the quarter
Adjusted net profit	11	222	113	(48.9)	968.8	• Key to FY2008 operating performance would be improvement in OPM as we do not expect revenue growth to pick up before 3QFY08
Operating profit margin (%)	7.1	15.3	11.5	—	—	• Expect investor focus on (a) client acquisition, which has been below the company's stated target of 8-9 new clients a quarter (b) slowdown in sub-prime mortgage clients (~9% of revenues)

(a) Result date yet to be announced by company; tentative date indicated based on past pattern for each company.

Source: Kotak Institutional Equities estimates.

Kotak Institutional Equities: Valuation summary of key Indian technology companies

Company	3-Jul-07 Price (Rs)	Rating	Mkt cap		EPS (Rs)			PER (X)			EV/EBITDA (X)			EV/Sales (X)		
			(Rs m)	(US\$ m)	2007	2008E	2009E	2007	2008E	2009E	2007	2008E	2009E	2007	2008E	2009E
HCL Technologies	335	IL	232,929	5,745	17.6	18.1	22.1	19.1	18.5	15.1	16.8	13.5	10.7	3.6	2.8	2.2
Hexaware Technologies	167	IL	23,764	586	8.9	11.5	14.4	18.8	14.6	11.6	15.4	10.7	7.9	2.4	1.7	1.3
i-flex solutions	2,586	U	215,413	5,313	33.2	51.0	74.2	77.8	50.8	34.9	58.1	36.3	25.4	10.2	7.8	6.2
iGate Global Solutions	307	U	9,718	240	15.7	22.5	30.0	19.6	13.6	10.2	10.4	7.0	5.0	1.2	0.9	0.7
Infosys Technologies	1,947	OP	1,117,607	27,566	67.0	83.8	103.4	29.1	23.2	18.8	24.0	18.6	14.2	7.6	5.7	4.3
Mindtree	773	IL	29,856	736	21.6	30.7	40.0	30.4	25.2	19.3	27.0	19.5	14.0	5.0	3.7	2.7
Mphasis BFL	327	IL	53,578	1,322	7.3	12.5	16.1	44.7	26.1	20.3	25.9	18.2	14.0	4.4	3.3	2.4
Polaris Software Lab	153	U	15,045	371	10.3	12.3	13.5	14.9	12.5	11.3	8.6	6.8	5.6	1.3	1.0	0.8
Satyam Computer Services	471	IL	316,343	7,803	21.4	26.4	32.0	22.0	17.9	14.7	18.1	13.9	10.4	4.3	3.2	2.4
TCS	1,128	IL	1,103,627	27,221	42.2	51.8	62.9	26.7	21.8	17.9	21.4	17.2	13.8	5.8	4.6	3.6
Tech Mahindra	1,427	IL	173,919	4,290	47.0	73.5	104.6	30.4	19.4	13.6	23.6	14.5	9.6	5.9	3.6	2.3
Wipro	515	OP	751,604	18,539	20.3	24.3	30.4	25.4	21.2	16.9	20.6	16.0	12.0	4.7	3.6	2.7
<b>Technology</b>		<b>Attractive</b>	<b>4,139,723</b>	<b>102,108</b>				<b>27.2</b>	<b>21.6</b>	<b>17.5</b>	<b>21.6</b>	<b>16.7</b>	<b>12.9</b>	<b>5.4</b>	<b>4.1</b>	<b>3.2</b>
<b>KS universe (b)</b>			<b>29,519,796</b>	<b>728,120</b>				<b>20.3</b>	<b>17.7</b>	<b>15.2</b>	<b>11.5</b>	<b>10.1</b>	<b>8.6</b>	<b>2.0</b>	<b>1.8</b>	<b>1.6</b>

Company	Target Price	(07P/E) / Egth	O/S Shares (m)	EPS Growth, %			Net Profit (Rs mn)			EBITDA (Rs mn)			Sales (Rs mn)		
				2007	2008E	2009E	2007	2008E	2009E	2007	2008E	2009E	2007	2008E	2009E
HCL Technologies	360	0.77	695	54.5	3.2	22.0	12,063	12,607	15,386	12,809	15,966	19,937	59,992	76,842	97,577
Hexaware Technologies	195	0.80	142	16.1	29.1	25.6	1,262	1,629	2,047	1,322	1,817	2,341	8,482	11,496	14,619
i-flex solutions	1,675	2.09	83	15.9	53.3	45.5	2,768	4,244	6,177	3,586	5,698	8,001	20,381	26,399	32,706
iGate Global Solutions	325	0.34	32	101.5	43.5	33.2	491	711	957	918	1,300	1,661	8,051	9,883	12,208
Infosys Technologies	2,300	0.91	574	48.7	25.1	23.5	37,530	48,203	59,526	43,910	55,434	70,445	138,930	180,064	232,106
Mindtree	750	1.29	39	17.1	41.9	30.4	892	1,231	1,594	1,086	1,492	2,039	5,904	7,938	10,548
Mphasis BFL	320	2.23	164	(21.5)	71.5	28.6	1,199	2,055	2,644	2,022	2,927	3,828	11,958	16,149	22,235
Polaris Software Lab	150	0.18	98	359.1	19.5	10.0	1,011	1,208	1,329	1,613	1,926	2,174	10,324	12,601	14,491
Satyam Computer Services	510	0.77	671	41.7	23.1	21.3	14,045.0	17,714.6	21,486.9	15,377.1	19,123.5	24,475.4	64,850.8	82,226.6	107,350.5
TCS	1,300	0.93	979	43.3	22.8	21.3	41,312	50,740	61,554	50,738	62,174	76,391	186,334	233,171	294,402
Tech Mahindra	1,850	(0.30)	122	124.3	56.5	42.3	6,184.9	9,585.1	13,640.7	7,367.3	11,857.7	17,215.0	29,290.0	47,395.3	70,731.1
Wipro	655	0.88	1,459	42.4	20.1	25.0	28,523	35,504	44,381	34,161	42,780	54,830	149,431	188,927	243,353
<b>Technology</b>				<b>47.1</b>	<b>25.7</b>	<b>23.2</b>	<b>152,397</b>	<b>191,574</b>	<b>236,032</b>	<b>181,636</b>	<b>230,569</b>	<b>290,427</b>	<b>727,237</b>	<b>930,880</b>	<b>1,188,757</b>
<b>KS universe (b)</b>				<b>35.8</b>	<b>14.3</b>	<b>16.5</b>									

Note

(a) HCL Technologies is June fiscal year-ending

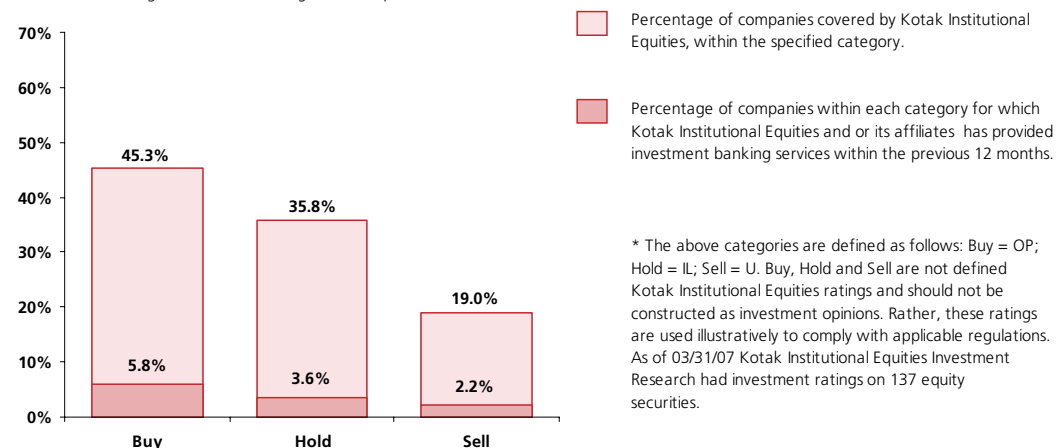
(b) Patni Computers Systems and Hexaware Technologies are December year-ending.

Source: Company reports, Kotak Institutional Equities estimates.

"I, Kawaljeet Saluja, hereby certify that all of the views expressed in this report accurately reflect my personal views about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report."

**Kotak Institutional Equities Research coverage universe**

Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities.

As of March 31, 2007

**Analyst coverage**

Companies that the analyst mentioned in this document follow

<b>Covering Analyst: Kawaljeet Saluja</b>	
<b>Company name</b>	<b>Ticker</b>
Bharti Airtel	BRTI.BO
HCL Technologies	HCLT.BO
Hexaware Technologies	HEXT.BO
Idea Cellular	IDEA.BO
i-flex solutions	IFLX.BO
iGate Global Solutions	MASC.BO
Infosys Technologies	INFY.BO
Mahanagar Telephone Nigam	MTNL.BO
MindTree Consulting	MINT.BO
Mphasis BFL	MBFL.BO
Patni Computer Systems	PTNI.BO
Polaris Software Lab	POLS.BO
Reliance Communications	RLCM.BO
Satyam Computer Services	SATY.BO
Tata Consultancy Services	TCS.BO
Tech Mahindra	TEML.BO
Videsh Sanchar Nigam	VSNL.BO
Wipro	WIPR.BO

Source: Kotak Institutional Equities Research.



## Ratings and other definitions/identifiers

### Current rating system

#### Definitions of ratings

**OP = Outperform.** We expect this stock to outperform the BSE Sensex over the next 12 months.

**IL = In-Line.** We expect this stock to perform in line with the BSE Sensex over the next 12 months.

**U = Underperform.** We expect this stock to underperform the BSE Sensex over the next 12 months.

#### Other definitions

**Coverage view.** The coverage view represents each analyst's overall fundamental outlook on the Sector. The coverage view will consist of one of the following designations: Attractive (A), Neutral (N), Cautious (C).

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