



Larsen & Toubro

STOCK INFO.	BLOOMBERG
BSE SENSEX: 19,243	LT IN
S&P CNX: 5,702	REUTERS CODE
	LART.BO

26 October 2007

Neutral

Previous Recommendation: Neutral

Rs3,877

Equity Shares (m)	283.3
52-Week Range	3,898/1,258
1,6,12 Rel. Perf. (%)	23/92/154
M.Cap. (Rs b)	1,098.1
M.Cap. (US\$ b)	27.8

YEAR	NET SALES	PAT*	EPS*	EPS	P/E*	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)*	(X)	(X)	(%)	(%)	SALES	EBITDA
3/07A	176,846	18,310	63.9	75.5	60.7	19.1	26.1	28.2	6.1	59.3
3/08E	237,648	25,261	88.1	36.3	44.0	15.6	30.4	33.4	4.6	37.9
3/09E	299,950	32,066	111.8	26.9	34.7	12.6	30.2	31.6	3.7	30.2

* Consolidated; EPS is fully diluted

- Robust 2QFY08 performance:** During 2QFY08, L&T reported revenues of Rs55b (up 47.2% YoY), EBIDTA of Rs4.7b (up 75.6% YoY) and net profit of Rs3.8b (up 140% YoY). The reported profit includes forex loss of Rs900m (due to Yen denominated loans). Adjusted net profit during 1QFY08 increased 59% YoY to Rs2.9b. Reported numbers are better than our estimates of revenues Rs47.8b, EBIDTA of Rs4.8b and net profit of Rs3b.
- EBIDTA margins improvement led by operational efficiency:** EBIDTA margins for 2QFY08 stood at 11.6% vs 8.9% in 2QFY07, up 268bps driven largely by operational efficiency and higher volumes. The margin improvement for the company is driven by 311bps improvement in E&C business to 11.7% (vs 8.6% YoY) while margins for the Machinery and Industrial Products (MIP) stood flat at 15.8% (vs 15.2% YoY). EBIDTA margins for Electronics and Electrical (E&E) division declined 32bps to 17.1% during 2QFY08 (vs 17.5% YoY) due to change in revenue mix.
- FY08 revenue guidance revised upwards:** The management has raised its revenue guidance for FY08 to 30-35% vs earlier guidance of 25-30%. The management however re-iterated that E&C division EBIDTA margin will be maintained or improve marginally. This is driven by strong order book position of Rs440b (2.5x FY07 revenues) vs Rs416b as of June 2007.
- Valuation and view:** We expect L&T to report consolidated net profit of Rs25.3b in FY08 (up 38% YoY) and Rs32.1b in FY09 (up 26.9% YoY). At CMP of Rs3,877/sh, the stock quotes at PER of 44x FY08 and 34.7x FY09E. Adjusted for the value of Ultratech Cemco (Rs40/sh) and L&T IDPL (Rs154/sh), the stock quotes at adj PER of 41.8x FY08 and 32.9x FY09. Maintain **Neutral**.

Y/E MARCH	QUARTERLY PERFORMANCE									
	FY07				FY08				(RS MILLION)	
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE	FY07	FY08E
Net Sales	34,689	37,361	41,184	62,482	45,052	54,999	53,613	82,686	175,788	236,350
Change (%)	11.5	11.7	12.3	36.0	29.9	47.2	30.2	32.3	20.0	34.5
EBITDA	2,698	3,062	5,185	9,718	4,738	6,526	6,817	12,865	20,665	30,946
Change (%)	53.5	117.6	63.0	54.2	75.6	113.1	31.5	32.4	82.4	60.7
As of % Sales	9.2	8.9	11.8	14.9	10.2	11.6	12.3	15.1	11.3	12.7
Depreciation	309	336	357	698	424	483	520	564	1,700	1,991
Interest	158	106	12	63	157	132	180	236	339	705
Other Income	216	437	350	420	1,608	-430	420	1,064	1,420	2,662
Reported PBT	2,448	3,057	5,166	9,377	5,764	5,481	6,537	13,131	20,046	30,913
Tax	877	1,046	1,727	2,371	1,995	2,001	2,157	4,345	6,019	10,499
Effective Tax Rate (%)	35.8	34.2	33.4	25.3	34.6	36.5	33.0	33.1	30.0	34.0
Reported Profit	1,571	2,011	3,440	7,006	3,769	3,480	4,380	8,785	14,027	20,414
Adjusted PAT	1,839	1,831	3,440	7,006	2,924	4,065	4,380	8,785	13,845	19,569
Change (%)	89.5	53.0	83.1	52.8	59.0	122.1	27.3	25.4	59.1	41.3

E: MOST; All quarterly numbers are for standalone entity

Robust 2QFY08 performance

During 2QFY08, L&T reported revenues of Rs55b (up 47.2% YoY), EBIDTA of Rs4.7b (up 75.6% YoY) and net profit of Rs3.8b (up 140% YoY). The reported profit includes forex loss of Rs900m (due to Yen denominated loans). Adjusted net profit during 1QFY08 increased 59% YoY to Rs2.9b. Reported numbers are better than our estimates of revenues Rs47.8b, EBIDTA of Rs4.8b and net profit of Rs3b.

EBIDTA margin improvement driven by operational efficiency

EBIDTA margins for 2QFY08 stood at 11.6% vs 8.9% in 2QFY07, up 268bps driven largely by operational efficiency and higher volumes. The margin improvement for the company is driven by 311bps improvement in E&C business to 11.7% (vs 8.6% YoY) while margins for the Machinery and Industrial Products (MIP) stood flat at 15.8% (vs 15.2% YoY). EBIDTA margins for Electronics and Electrical (E&E) division declined 32bps to 17.1% during 2QFY08 (vs 17.5% YoY) due to change in revenue mix. The robust improvement in EBIDTA margin for E&C division was largely driven by operational efficiency and better project execution.

FY08 revenue guidance revised upwards

The management has raised its revenue guidance for FY08 to 30-35% vs earlier guidance of 25-30%. The management however re-iterated that E&C division EBIDTA margin will be maintained or improve marginally. This is driven by strong order book position of Rs440b (2.5x FY07 revenues) vs Rs416b as of June 2007.

Robust order backlog, Order intake momentum continues

The order backlog for the company continues to be robust at Rs440b (2.5x FY07 revenues) vs Rs416b as of June 2007 and Rs307b in Sept 2006. The order booking too grew by robust 26.4% YoY during 2QFY08 to Rs75.5b in 2QFY08 (vs Rs59.7b in 2QFY07). The significant part of the incremental orders for the company was largely from the Hydrocarbon and Infrastructure segments.

E&C Business: strong margin improvement

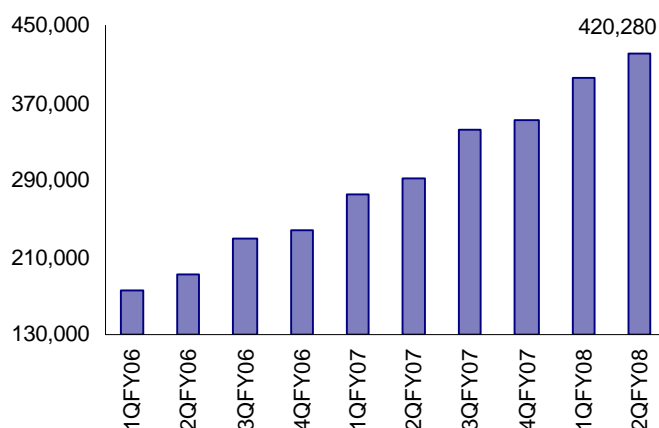
During 2QFY08, E&C business reported revenues of Rs41.1b (vs Rs27b in 2QFY07), while EBIDTA margins improved to 11.7% vs 8.6% in 2QFY07. EBIDTA for the quarter grew by robust 107% YoY to Rs4.8b (vs Rs2.3b in 2QFY07). During 2QFY08, order intake stood of Rs59.1b, up 27.5% YoY; and order backlog increased to Rs420.3b, up from Rs292.7b in 2QFY07 and Rs396.9b in 1QFY08.

L&T - E&C DIVISION PERFORMANCE (RS M)

	2QFY07	3QFY07	4QFY07	1QFY08	2QFY08	% YOY
Order Intake	46,310	81,720	61,200	82,180	59,050	27.5
Domestic	37,860	71,610	44,430	65,470	43,960	47.4
Export	8,450	10,110	16,780	16,710	15,090	78.6
Order Backlog	292,700	341,420	353,330	396,900	420,280	43.6
Net Sales	26,970	30,360	48,150	33,220	41,080	52.3
EBITDA	2,320	3,460	7,090	3,190	4,810	107.3
EBITDA Mar. (%)	8.6	11.4	14.7	9.6	11.7	

Source: Company

E&C DIVISION ORDER BACK LOG (RS M)



Source: Company

ORDER BOOK COMPOSITION (%)

	FY03	FY04	FY05	FY06	FY07	1HFY08
Process Inds.	17	16	14	10	12	13
Oil & Gas	21	23	19	24	19	20
Power	10	10	23	17	16	12
Infrastructure	35	33	31	31	39	36
Others	17	18	13	18	14	19
Total	100	100	100	100	100	100

Source: Company

EBG business: strong revenue growth

The Electricals Business Group registered a healthy 43.4% YoY growth in revenues, driven by switchgears while EBIDTA margins declined by 32bps to 17.1%. Standard products now account for 60% of the revenues of the division.

L&T – EBG DIVISION PERFORMANCE (RS M)

	FY07				FY08		YOY
	1Q	2Q	3Q	4Q	1Q	2Q	%
Sales	3,820	4,350	4,420	5,860	5,030	6,240	43.4
EBITDA	690	760	750	990	840	1,070	40.8
EBITDA Mar. (%)	18.1	17.5	17.0	16.9	16.7	17.1	

Source: Company

MIP business: strong growth in revenue and EBIDTA

The Machinery and Industrial Parts (MIP) Business Group registered a strong revenue growth of 29.5% YoY and 62bp improvement in EBIDTA margins to 15.8%. The segment comprises of marketing income of valves, rubber processing, machinery, welding, paper machinery, construction equipments, etc,

L&T – MIP DIVISION PERFORMANCE (RS M)

	FY07				FY08		YOY
	1Q	2Q	3Q	4Q	1Q	2Q	%
Sales	3290	4,355	4,000	6420	4170	5640	26.7
EBITDA	600	660	570	1400	920	890	53.3
EBITDA Mar. (%)	18.2	15.2	14.3	21.8	22.1	15.8	

Source: Company

L&T Infotech – EBIDTA margin improvement led by higher productivity

L&T Infotech's operational performance was satisfactory, with 2QFY08 revenues of Rs3.9b (up 18% YoY) and Net Profit of Rs570m (up 39% YoY). During 2QFY08, PAT margins for the company was higher by 223bps to 14.7% (vs 12.5%), due to improving productivity. The revenue growth in USD stood at robust 37% YoY and revenues from US constituted to 73% of total revenues. The total number of employees for the company increased to 8,794 in 2QFY08 vs 6,777 in 2QFY07 and 7,220 in 4QFY07.

L&T INFOTECH PERFORMANCE (RS M)

	2QFY08	2QFY07	% YOY	1QFY07	% QOQ
Revenues	3,870	3,280	18.0	3,630	6.6
PAT	570	410	39.0	430	32.6
PAT (%)	14.7	12.5		11.8	

Source: Company

Progress on BOT projects

L&T Infrastructure Development Projects (L&T IDPL) currently has 36 projects (14 operational), vs 33 projects during 1QFY08 (14 operational). The total cost of all the projects is Rs186b while the equity invested in all the projects totaled to 12.1b. L&T Urban Infrastructure now has 33m sq.ft under development (vs 22m sq.ft as at Mar 07), and total project cost stands at Rs94b (vs Rs67b in Mar 07).

PROJECT PORTFOLIO AS OF JUNE 2007 (RS B)

SECTOR	OPERA-	UNDER	PROJECT	REMARKS
	TIONAL	IMPL.	COST	
	(NOS)	(NOS)		
Roads & Bridges	4	5.0	43	1,480 lane kms
Ports	2	1.0	30	33m tons
Urban Infrastructure	8	12.0	90	33m sq ft
Airports	-	1.0	19	23m passengers
Total Project Cost			182	
Equity Invested			12	

Source: Company

Valuation and view

We now expect L&T to report consolidated net profit of Rs25.3b in FY08 (up 38% YoY) and Rs32.1b in FY09 (up 26.9% YoY). Our EPS estimates are being upgraded by 4.4% for FY08 to Rs88.1 (up 36.3% YoY) and by 4.7% for FY09 to Rs111.8 (up 26.9% YoY). We arrive at Price Target of Rs3023/sh based on sum of parts methodology: core business Rs2,221/sh (25x FY09 PER), L&T Infotech at Rs198/sh (15x FY09PER), L&T Infrastructure Development Projects Rs154/sh, Ultratech Cemco stake at Rs40/sh (25% discount to current price), L&T Finance Rs62/sh (15x FY09PER), International Ventures at Rs151/sh and Manufacturing Ventures at Rs167/sh.

At CMP of Rs3,877/sh, the stock quotes at PER of 44x FY08 and 34.7x FY09E. Adjusted for the value of Ultratech Cemco (Rs40/sh) and L&T IDPL (Rs154/sh), the stock quotes at adj PER of 41.8x FY08E and 32.9x FY09E. Maintain **Neutral**.

L&T: SUM OF PARTS VALUE

	BUSINESS SEGMENT	METHOD	VALUATION (X)	VALUE (RS M)	VALUE (RS/SH)	RATIONALE
L&T Standalone	Engineering, Construction, & Electricals	FY09E PER (x)	25	603,481	2,221	Premium to industry average
Ultratech Cement (11.5% stake)	Cement	Discount to Current Price (Rs/sh)	758	10,853	40	20% discount to current price
L&T Infotech (100% stake)	Infotech	FY09E PER (x)	15	53,888	198	Discount to niche second tier IT companies
L&T Infrastructure Dev. Projects Ltd.	Infrastructure	Benchmark price		41,970	154	Based on 50% discount of benchmark price (recent stake sale to strategic investors)
L&T Power Investments Pvt Ltd						
- HPL Co Generation	Captive Power Projects	FY09E PER (x)	15	7,443	27	Discount to sector average PER
- India Infrastructure Developers	Captive Power Projects	FY09E PER (x)	15	803	3	Discount to sector average PER
L&T Finance (100% stake)	Hire Purchase, Leasing, Bill Discounting	FY09E PER (x)	15	16,770	62	In line with industry average L&T has advantage of catering to in house requirement of L&T's dealers / vendors / customers, etc
International Ventures						
- L&T (Oman) Llc	EPC projects in Oman	FY09E PER (x)	20	12,155	45	Discount to L&T's valuations
- L&T Saudi Arabia Llc	EPC projects in Saudi Arabia	FY09E PER (x)	20	6,000	22	Discount to L&T's valuations
- Zubair Kilpatrick Llc	Electrical and Instrumentation for Oil / Gas	FY09E PER (x)	20	1,791	7	Discount to L&T's valuations
- L&T International FZE	Commodity Hedging	FY09E PER (x)	20	21,039	77	Lower PER, given risks in commodity hedging
Manufacturing Ventures						
- L&T Komatsu	Excavators and Hydraulic System	FY09E PER (x)	20	20,598	77	In line with industry average
- Audco India	Industrial Valves	FY09E PER (x)	20	16,868	62	Revenue growth and margins have shown strong consistency
- EWAC Alloys	Welding	FY09E PER (x)	20	7,492	28	In line with industry average
Total				3,023		

Larsen & Toubro: an investment profile

Company description

L&T is India's largest engineering and construction company. It undertakes projects on engineering, procurement and commissioning basis. Its business is categorized in three segments, viz. Engineering and construction (E&C), Electrical and Electronics (E&E) and other diversified businesses. It has demerged its cement and other non-core businesses and emerged as a focused engineering player offering a comprehensive exposure to Indian industry and infrastructure. It has many subsidiaries and associate companies which will gradually start adding robustly to its bottom-line.

Key investment arguments

- ✍ L&T is witnessing increased traction in order inflows. Management has guided for 30-35% YoY growth in revenues in FY08.
- ✍ We are also excited about the growth opportunity and L&T's positioning in high end segments like nuclear, defence and aerospace.
- ✍ We believe that L&T's subsidiaries, particularly infrastructure and Infotech, can unlock sizeable value going forward.
- ✍ During FY07-09, we expect L&T's to report a 32% consolidated earnings CAGR.

COMPARATIVE VALUATIONS

		L&T	SIEMENS**	ABB*
P/E (x)	FY08E	44.0	55.7	60.2
	FY09E	34.7	38.3	46.6
P/BV (x)	FY08E	15.6	20.8	27.9
	FY09E	12.6	16.4	22.1
EV/Sales	FY08E	4.6	3.3	4.9
	FY09E	3.7	2.4	3.7
EV/EBIDTA	FY08E	37.9	34.8	39.5
	FY09E	30.2	25.3	30.1

* December Ending ; ** September Ending

SHAREHOLDING PATTERN (%)

	SEP-07	JUN-07	SEP-06
Promoter	0.0	0.0	0.0
Domestic Inst	37.2	38.2	36.5
Foreign	22.4	21.2	21.1
Others	40.5	40.6	42.4

Key investment concerns

- ✍ Higher borrowings warranted for investments in SPVs
- ✍ Liabilities in terms of cost over runs and other failures may arise on the international projects

Recent developments

- ✍ L&T has agreed to buy out the switchgear business of Tamco in Malaysia for US\$108 m.

Valuation and view

- ✍ L&T offers the best play on the Indian Infrastructure and industry. Increased momentum in order intake, value unlocking probability from subsidiaries and increasing share of high margin businesses would drive re-rating.

Sector view

- ✍ Investments in manufacturing industries are likely to gain momentum as operating at peak utilization rates.
- ✍ Government thrust on infrastructure and allotment of projects on BOT basis is positive for larger players.

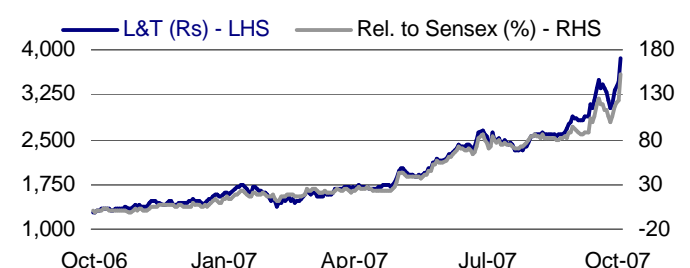
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY08	88.1	78.7	11.9
FY09	111.8	102.6	9.0

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
3,877	3,023	-	Neutral

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT					
(Rs Million)					
Y/E MARCH	2005	2006	2007	2008E	2009E
Total Revenues	134,363	150,546	180,064	241,972	305,408
Growth Rate (%)	35.4	2.0	19.6	34.4	26.2
Excise Duty	1,768	2,308	3,218	4,324	5,458
Net Revenues	132,595	148,239	176,846	237,648	299,950
Growth Rate (%)	37.0	11.8	19.3	34.4	26.2
Manufacturing Expenses	105,161	115,903	130,782	172,475	217,568
Staff Cost	7,645	8,900	12,582	15,728	19,660
S G & A Expenses	10,961	12,170	14,992	20,084	25,349
EBITDA	8,828	11,266	18,490	29,361	37,373
Change (%)	57.4	27.6	64.1	58.8	27.3
EBITDA Margin (%)	7.5	9.6	12.2	13.6	13.5
Depreciation	926	1,141	1,682	1,991	2,965
EBIT	7,902	10,125	16,809	27,370	34,408
Net Interest	536	751	339	705	1,169
Recurring Other Income	1,261	2,061	3,031	2,883	3,200
Non-recurring Other Income	4,028	1,622	470	0	0
Add: Trf to Revaluation R	15	15	14	14	14
Share from Subsidiaries	191	64	64	65	65
Profit before Tax	12,861	13,137	20,048	29,627	36,519
Tax	3,023	3,713	6,019	10,044	12,380
Effective Tax Rate (%)	23.5	28.3	30.0	33.9	33.9
Reported Profit	9,838	9,424	14,030	19,583	24,139
Extra-ordinary Adjustment	4,028	1,622	470	0	0
Adjusted Profit	5,811	7,802	13,560	19,583	24,139
Growth (%)	12.1	34.3	73.8	44.4	23.3
Consolidated Profit	6,408	10,302	18,310	25,261	32,066
Growth (%)	8.4	60.8	77.7	38.0	26.9

BALANCE SHEET					
(Rs Million)					
Y/E MARCH	2005	2006	2007	2008E	2009E
Equity Capital	260	275	567	574	574
Reserves and Surplus	33,432	46,127	57,118	70,823	87,716
Net Worth	33,691	46,402	57,684	71,396	88,290
Debt	18,591	14,536	20,778	30,454	47,454
Deferred Tax Liability	945	773	402	402	402
Capital Employed	53,227	61,710	78,864	102,252	136,146
Gross Fixed Assets	21,066	23,007	28,763	41,475	56,475
Less : Depreciation	10,895	9,822	11,159	13,150	16,115
Add : Capital WIP	658	2,861	4,712	3,000	3,000
Net Fixed Assets	10,831	16,046	22,316	31,325	43,360
Investments	9,609	19,195	31,044	45,044	57,044
Inventory	23,108	22,103	30,011	39,776	50,204
Sundry Debtors	39,636	48,142	55,046	74,249	92,041
Cash & Bank	8,280	5,832	10,944	4,006	5,619
Loans & Advances	17,318	19,116	22,579	29,832	37,653
Other Current Assets	40	173	196	0	0
Current Assets	88,382	95,365	118,778	147,863	185,517
Current Liabilities	55,994	69,116	93,373	121,980	149,776
Net Current Assets	32,388	26,249	25,405	25,883	35,741
Miscellaneous Expenditur	399	220	98	0	0
Capital Deployed	53,227	61,710	78,864	102,252	136,146

E: MOST Estimates

RATIO					
Y/E MARCH	2005	2006	2007	2008E	2009E
Basic (Rs)					
Adjusted EPS	22.4	56.8	47.9	68.3	84.2
Consolidated EPS	24.7	75.0	64.6	88.1	111.8
Con. EPS (Fully Dilut	24.7	36.4	63.9	88.1	111.8
Growth (%)	3.8	47.5	75.5	38.0	26.9
Cash Earning per Share	23.9	31.6	53.9	76.2	95.7
Book Value	256.3	336.1	203.3	249.0	307.9
Dividend Per Share	27.5	22.0	13.0	17.8	21.9
Div. Payout (Incl. Div Tax)	41.3	36.6	30.1	30.0	30.0
Valuation (x)					
P/E (Standalone)		68.3	81.0	56.8	46.1
P/E (Consolidated)		51.7	60.0	44.0	34.7
P/E (Consolidated) (Fully Diluted)		106.6	60.7	44.0	34.7
Price / CEPS		122.5	71.9	50.9	40.5
EV/EBITDA		97.6	59.3	37.9	30.2
EV/ Sales		7.3	6.1	4.6	3.7
Price / Book Value		11.5	19.1	15.6	12.6
Dividend Yield		0.6	0.3	0.5	0.6
Return Ratio (%)					
RoE	19.2	19.6	26.1	30.4	30.2
RoCE	19.2	21.2	28.2	33.4	31.6
Turnover Ratios					
Debtors (Days)	107.7	116.7	111.6	112.0	110.0
Inventory (Days)	62.8	53.6	60.8	60.0	60.0
Asset Turnover (x)	2.5	2.4	2.3	2.4	2.2
Leverage Ratio					
Current Ratio (x)	16	14	13	12	12
D/E (x)	0.6	0.3	0.4	0.4	0.5

CASHFLOW STATEMENT					
(Rs Million)					
Y/E MARCH	2005	2006	2007	2008E	2009E
PBT before EO Items	12,861	13,137	20,048	29,627	36,519
Add : Depreciation	957	1,160	1,715	1,991	2,965
Interest	536	751	339	705	1,169
Less : Direct Taxes Paid	3,023	3,713	6,019	10,044	12,380
(Inc)/Dec in WC	-6,018	3,691	5,887	-7,347	-8,246
CF from Operations	5,313	15,026	21,971	14,932	20,027
(Inc)/Dec in FA	-1,624	-6,375	-7,984	-11,000	-15,000
(Pur)/Sale of Investments	50	-9,586	-11,849	-14,000	-12,000
CF from Investments	-1,574	-15,961	-19,834	-25,000	-27,000
(Inc)/Dec in Networth	38	6,740	1,219	105	0
(Inc)/Dec in Debt	5,347	-4,055	6,173	9,677	17,000
Less : Interest Paid	536	751	339	705	1,169
Dividend Paid	4,061	3,446	4,216	5,878	7,246
CF from Fin. Activity	788	-1,512	2,906	3,198	8,585
Inc/Dec of Cash	4,528	-2,448	5,043	-6,869	1,613
Add: Beginning Balance	3,753	8,280	5,832	10,944	4,006
Closing Balance	8,280	5,832	10,944	4,006	5,619

N O T E S



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1. Analyst ownership of the stock	No
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