Company Flash

28 November 2007 | 6 pages

DLF (DLF.BO)

Buy: Increasing Hotel Exposure, Acquires Stake in Aman Resorts

- **50% stake in high-end luxury hotel chain** — DLF has formed an equal partnership with the founder of Aman Resorts to acquire the company at an EV of US$400m (including debt of US$150m). While this appears aggressive, it includes an agreement to acquire a controlling interest in Aman Resort. The acquisition will be largely financed through plans to raise debt.

- **About Aman Resorts** — This is a luxury hotel chain operating 22 hotels (650 keys), many with villas (172 keys). It owns properties in France, Phuket, Bali, Indonesia, Sri Lanka and India, which are awarded. Its customer mix is broad-based: 34% from EU, 34% from Asia-Pacific and 28% from US. DLF would work closely with founder Adrian Zecha for driving growth ahead.

- **Healthy growth forecasted for Aman** — Aman enjoys ARRs of US$778-1,000 and is likely to generate CY07 revs of US$120m with EBITDA of US$27m. With six new properties (300 keys, fully funded) in various stages of development likely to go operational by 08-09, management expects to grow earnings at 20% and believe DLF's land bank and growth capital would complement this.

- **Impact** — Acquisition is in-line with DLF's plans to grow big in the hotel space. While the acquisition at 15x CY07E EV/EBITDA appears aggressive vs. 10x EV/EBITDA for most global hotel chains, we believe Aman Resorts has inherent value of real estate assets which should add significant value in the long-term (e.g. owns a hotel site at Lodhi Road, Central Delhi for upcoming luxury hotel with ~68 suites). Given the limited data, we have not built this in our NAV.

Buy/Medium Risk	1M
Price (28 Nov 07)	Rs879.50
Target price	Rs1,046.00
Expected share price return	18.9%
Expected dividend yield	0.7%
Expected total return	**19.6%**
Market Cap	Rs1,499,400M US$37,802M

Price Performance (RIC: DLF.BO, BB: DLFU IN)

Statistical Abstract

Year to 31 Mar	Net Profit (RsM)	Diluted EPS (Rs)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2006A	1,917	12.34	100.2	71.3	14.4	22.6	0.0
2007A	19,413	12.80	3.7	68.7	44.2	97.9	0.0
2008E	69,431	40.73	218.1	21.6	8.3	65.7	0.7
2009E	99,170	58.17	42.8	15.1	5.6	44.3	0.9
2010E	129,661	76.05	30.7	11.6	4.0	40.1	1.1

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

[1]Citigroup Global Markets India Private Limited

DLF

Company description

DLF is one of India's oldest real estate developers. Established in Delhi in 1946, it has continued to expand and diversify its real estate businesses, and is among the largest developers in India. It has historically built its businesses in Delhi and adjoining areas, know as the National Capital Region (NCR). DLF has diversified into other geographic locations over the last few years. These expansions are spread across India, with a particular focus on the Northern India belt, Kolkata, Mumbai, Chennai, and a number of other large and rapidly growing cities. DLF enjoys a strong brand franchise with good reputation in execution and delivery. This is the flagship company of the KP Singh family with the founders holding ~90% (post the recent primary offering in Jul'07 at Rs525). It is amongst India's largest developers with diversified asset portfolio and an emerging pan-India presence.

Investment strategy

We rate DLF shares Buy / Medium Risk (1M), with a target price of Rs1,046 based on a 25% premium to our NAV estimate of Rs837 which includes other asset holding/JV businesses of Rs75. DLF's focus on scale, integrated development with execution record, and a large land holding spread across top-tier growth cities differentiates it from its peers. Its diversified portfolio of ~738m sq ft is relatively leveraged toward commercial/IT Parks/Retail mall (33% of total development) assets, which should provide a good hedge particularly in the near-term, when the residential segment is seeing some slowdown. We believe it is a good proxy to play potential yield compression. While the stock has had a solid 53% run over last 3-m, we see further upside. Potential listing of DLF Office Trust in Singapore would generate positive sentiment for the stock, in our view. We see this as a core holding for playing the Indian real estate sector.

Valuation

Our target price of Rs1,046 is based on a 25% premium to our core NAV and other asset holding/JV estimate of Rs837. This includes Rs762 for the development portfolio and Rs75 for other asset holdings and new JV businesses (Rs45/share for the existing 4.6m sq ft of leased assets and 7.2m sq ft of plots, and Rs30/share for DLF's share in construction and hotel JVs). The premium is attributed to - 1) diversified tier-I developer with large land bank, 2) high leverage towards office/IT Parks and retail assets; 3) relatively de-leveraged balance sheet, and 4) strong track record that provides it with potential to win large township projects. We believe an NAV-based valuation methodology is most appropriate for developers, as it factors the varied development projects and spread out time frame.

Our NAV estimate of Rs837 is based on the following assumptions: 1) current market prices will persist, without any price inflation; 2) development volume of 701m sq ft (as ~43m is already/to be recognized as revenue till Sep '08); 3) a cap rate of 9% for commercial/IT Park, IT SEZs in Super Metros and Metros, and 10% for other locations; 4) all projects undertaken by DLF will be completed largely on schedule; though given the scale, we expect risk of delays; 5) average cost of capital of 14%; and 6) a tax rate of 25%.

Risks

We rate DLF shares Medium Risk. This is different from the Speculative Risk rating assigned by our quantitative risk-rating system to stocks that have less than one year's trading history. The key reasons for assigning a Medium Risk rating include: 1) the company's robust business model; 2) pan-India land bank with initiatives to de-risk the business model through new business JVs; and 3) relatively healthy cash flows, at a time when most developers are facing funding constraints.

The main risks to our investment thesis and to the shares reaching our target price include:

The company's asset sale strategy remains contingent on capital flows, especially with the government exploring measures to regulate FDI in the sector. Outstanding from DLF Assets is high at Rs.20bn, and evolving regulatory issues on REITs/Trust could potential delay planned listing of DLF Office Trust; any delays in the listing DLF Office Trust could be a negative sentiment for the stock.

Poor response for its mid-income housing projects expected to launch in 3Q/4Q; a good response is crucial for growth ahead and cash flows, but the demand environment in the residential market remains sluggish.

Slowdown in the IT/ITES industry which could lead to a decline in demand for commercial real estate. While there is strong demand for IT space, in event of the sector facing a slowdown, DLF could get adversely impacted due to its high leverage and scale.

Slowdown in capital inflows or measures to regulate FDI in the real estate sector.

Appendix A-1

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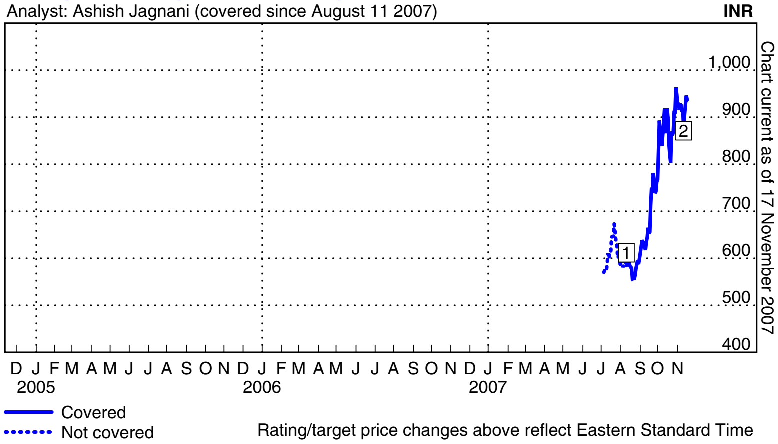
DLF (DLF.BO)
Ratings and Target Price History - Fundamental Research
Analyst: Ashish Jagnani (covered since August 11 2007)



#	Date	Rating	Target Price	Closing Price
1:	10 Aug 07	1M	725.00	584.45
2:	12 Nov 07	1M	*1,046.00	871.20

*Indicates change.

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