kotak® Institutional Equities

INDIA DAILY

May 18, 2007

EQUITY MARKETS

India	17-May	1-day	1-mo	3-mo
		Change, %		
Sensex	14,300	1.2	4.6	(0.4)
Nifty	4,220	1.2	5.2	1.8
Global/Regional indices				
Dow Jones	13,477	(0.1)	5.3	5.6
Nasdaq Composite	2,539	(0.3)	1.2	1.7
FTSE	6,579	0.3	2.0	2.5
Nikkie	17,467	(0.2)	(1.1)	(2.3)
Hang Seng	20,810	(0.9)	0.2	1.2
KOSPI	1,601	(0.9)	4.3	10.5

Value traded - India

	17-May		1-mo	3-mo
			Moving avg, Rs bn	
Cash (NSE+BSE)	181.4		136.5	125.2
Derivatives (NSE)	366.7		297.5	405.0
Deri. open interest	572.9		562.0	620.6

Contents

Results

Tata Steel: 4Q results in line with expectations; maintain U

Bajaj Auto: Maintain OP with a target of Rs2,780 despite lower effective stake in insurance ventures

Max India: Insurance is the key driver; stock seems expensive

Forex/money market

	17-May	1-day	1-mo	3-mo
		Change, basis points		
Rs/US$	40.8	-	(117)	(329)
6mo fwd prem, %	0.7	(25)	71	24
10yr govt bond, %	8.2	-	2	9

Net investment (US$mn)

	16-May		MTD	CYTD
FIIs	(33)		1,257	40
MFs	82		236	(303)

Top movers -3mo basis

Best performers	17-May	1-day	1-mo	3-mo
		Change, %		
Balaji Telefilms	202	3.4	21.5	56.2
Thomas Cook	70	2.7	41.0	44.5
Reliance Cap	901	7.6	27.7	30.7
Castrol India	283	(1.4)	17.8	26.1
SAIL	141	0.3	12.0	23.8
Worst performers				
Polaris	172	2.2	(10.8)	(22.8)
Wipro	545	0.9	(7.1)	(19.4)
M&M	728	1.1	(2.3)	(19.2)
Ashok Leyland	37	(0.8)	(0.8)	(18.5)
Cipla	208	(0.7)	(10.6)	(18.2)

News Roundup

Corporate

- The board of Bajaj Auto (BAL) approved the planned demerger of the company creating three different entities – Bajaj Auto Ltd (BAL), Bajaj Holdings and Investment Company (BHIL), and Bajaj Finserv Limited (BFL). Bajaj Holdings and Investment Ltd (which will be the new auto company) will be renamed Bajaj Auto Ltd and the existing Bajaj Auto Ltd will be known as Bajaj Holdings and Investment Ltd, (which will act as the primary investment company). Both BHIL and BFL will be listed on the bourses by the end of this year. (FE)
- Idea Cellular, an Aditya Birla Group company, signed a US$500 mn network expansion deal with Nokia Siemens Networks. The pact will enable the GSM service provider to expand its network in the country. (BS)
- Suzlon Energy has issued zero-coupon foreign currency convertible bonds worth US$300 mn to part-finance its organic growth initiatives. (BS)
- HDFC Bank has announced a capital raising plan amounting US$1 bn—or Rs 4,200 crore—whichever is higher, through a combination of domestic and international issues to fund growth. (FE)

Economic and political

- Recognising the threat of hardening international non-fuel commodity prices on inflation, the department of economic affairs in the Union finance ministry has suggested aggressive sterilisation of foreign capital inflows, tightening of government expenditure and intervention in key farm produce markets like wheat. (BS)
- The capacity addition for the power sector has been revised downward by 43.4% to 23, 250.24 MW, from the original target of 41,110 MW as shown in the ministry's website. The latest figure is 37% lower than the earlier estimate of 36,956 MW as well. (FE)report and, in so far as it includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line.

Kotak Institutional Equities Research
kotak.research@kotak.com
Mumbai: +91-22-6634-1100

Metals

TISC.BO, Rs597	
Rating	U
Sector coverage view	Neutral
Target Price (Rs)	400
52W High -Low (Rs)	609 - 377
Market Cap (Rs bn)	464.5

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	174.0	182.2	195.2
Net Profit (Rs bn)	44.3	38.1	35.2
EPS (Rs)	74.8	75.5	61.9
EPS gth	*11.7*	*1.0*	*(18.0)*
P/E (x)	8.0	7.9	9.6
EV/EBITDA (x)	5.7	5.2	6.0
Div yield (%)	1.9	2.5	2.5

Shareholding, March 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	30.5	-	-
FIIs	17.4	0.8	(0.2)
MFs	3.2	0.9	(0.1)
UTI	-	-	(0.9)
LIC	12.0	2.9	2.0

Tata Steel: 4Q results in line with expectations; maintain U

Abhijeet Naik : abhijeet.naik@kotak.com, +91-22-6634-1220

Amit Agarwal : agarwal.amit@kotak.com, +91-22-6749-3390

- **Corus reports improves 1Q EBITDA due to strong steel prices**
- **Maintaining EPS estimates and Underperform rating on the stock**

Tata Steel reported 4Q net profit at Rs11.0 bn (41% yoy growth) and in-line with our estimate of Rs11.5 bn. 4Q EBITDA at Rs19.0 bn, too, was in line with our estimate of Rs19.5 bn. 4Q EBITDA margin at 38.2% rose 670 bps yoy but declined 170 bps qoq. Lower-than-expected other income and lower-than-expected interest costs, too, accounted for the variation vis-'-vis our profit estimates. Finished steel sales for 4Q at 1.26 mn tons rose 2% qoq. Average net steel realizations in 4Q grew 22% yoy and 9% qoq. We expect realizations to remain stable at these levels due to firm steel prices.

Corus reports improves 1Q EBITDA due to strong steel prices

In 1QCY2007, Corus has reported a recurring EBITDA of 254 mn pounds ' a 76% jump over 1QCY2006 level of recurring EBITDA on the back of strong steel prices (+8-10% yoy). EBITDA margins have improved to 9.4% Vs 6.2% last year. However, even a slight drop in steel prices in Europe could return EBITDA margins to CY2006 levels, in our opinion.

Maintaining EPS estimates and Underperform rating on the stock

In our view, sensitivity of Tata Steel's cons profits to steel prices has increased significantly post the Corus acquisition. A 10% change in steel prices could change cons profits by as much as 50%. Given that European steel prices are currently at an all-time-high, we see risk-reward as unfavorable at current levels. We maintain our EPS estimates and Underperform rating on the stock.

Tata Steel: 4QFY2007 results

	Stand-alone			% chg.		Kotak estimates		Consolidated		
(in Rs mn)	4QFY06	3QFY07	4QFY07	qoq	yoy	4QFY07	% deviation	FY06	FY07	% chg.
Net sales	**41,290**	**44,700**	**49,804**	**11.4**	**20.6**	**48,275**	**3.2**	**151,394**	**175,520**	**15.9**
Operating costs	**(28,282)**	**(26,864)**	**(30,769)**	**14.5**	**8.8**	**(28,734)**	**7.1**	**(92,079)**	**(105,788)**	**14.9**
(Incr)/Decr in stocks	(1,607)	790	(654)	(182.8)	(59.3)	50	(1,397.8)	1,049	825	(21.4)
Consumption of RM	(8,794)	(9,425)	(9,712)	3.0	10.4	(9,779)	(0.7)	(30,244)	(35,721)	18.1
Staff Cost	(3,725)	(3,611)	(4,297)	19.0	15.3	(3,858)	11.4	(13,530)	(14,568)	7.7
Power	(2,290)	(2,261)	(2,415)	6.8	5.5	(2,365)	2.1	(8,192)	(9,217)	12.5
Freight & Handling	(2,811)	(2,856)	(2,987)	4.6	6.3	(3,050)	(2.1)	(10,043)	(11,175)	11.3
Other Expenditure	(9,055)	(9,502)	(10,705)	12.7	18.2	(9,732)	10.0	(31,119)	(35,932)	15.5
EBITDA	**13,008**	**17,836**	**19,035**	**6.7**	**46.3**	**19,540**	**(2.6)**	**59,315**	**69,733**	**17.6**
Other income	644	987	798	(19.2)	23.9	906	(12.0)	2,548	4,337	70.2
Interest costs	(172)	(520)	(448)	(13.9)	161.3	(563)	(20.4)	(1,184)	(1,739)	46.8
Depreciation	(1,933)	(1,991)	(2,294)	15.2	18.7	(2,045)	12.2	(7,751)	(8,193)	5.7
Extraordinairies: VRS costs	344	(493)	(401)	(18.6)	(216.7)	(516)	(22.3)	(528)	(1,521)	188.2
PBT	**11,891**	**15,820**	**16,690**	**5.5**	**40.4**	**17,322**	**(3.6)**	**52,400**	**62,617**	**19.5**
Taxes	(4,060)	(5,183)	(5,655)	9.1	39.3	(5,816)	(2.8)	(17,336)	(20,395)	17.6
PAT	**7,831**	**10,638**	**11,035**	**3.7**	**40.9**	**11,506**	**(4.1)**	**35,064**	**42,222**	**20.4**
Key metrics										
EBITDA margin (%)	31.5	39.9	38.2	(1.7)	6.7	40.5		39.2	39.7	0.5
PAT margin (%)	19.0	23.8	22.2	(1.6)	3.2	23.8		23.2	24.1	0.9
Effective tax rate (%)	34.1	32.8	33.9	1.1	(0.3)	33.6		33.1	32.6	(0.5)
Avg. net realisation (Rs/ton)	28,849	32,236	35,135	9.0	21.8					
Production and sales data										
Production (mn tons)	1.26	1.29	1.27	(1.4)	0.9	1.29		4.55	4.95	8.6
Sales volume (mn tons)	1.26	1.23	1.26	2.1	0.4	1.27		4.42	4.80	8.6

Source: Company data, Kotak Institutional Equities

Automobiles

BJAT.BO, Rs2500	
Rating	OP
Sector coverage view	Attractive
Target Price (Rs)	2,780
52W High -Low (Rs)	3259 - 2085
Market Cap (Rs bn)	253.0

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	93.9	104.4	120.0
Net Profit (Rs bn)	12.5	13.7	15.8
EPS (Rs)	118.2	130.3	151.5
EPS gth	*8.6*	*10.2*	*16.3*
P/E (x)	21.2	19.2	16.5
EV/EBITDA (x)	10.1	9.3	7.7
Div yield (%)	1.6	2.0	2.4

Shareholding, March 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	29.8	-	-
FIIs	21.5	0.9	0.0
MFs	2.0	0.5	(0.4)
UTI	-	-	(0.9)
LIC	3.0	0.7	(0.2)

Bajaj Auto: Maintain OP with a target of Rs2,780 despite lower effective stake in insurance ventures

Abhijeet Naik : abhijeet.naik@kotak.com, +91-22-6634-1220
Amit Agarwal : agarwal.amit@kotak.com, +91-22-6749-3390

- **4Q net profit at Rs3.1 bn falls 11% yoy, operating performance in-line with estimates**
- **De-merger announcement will likely lead to unlocking of value**
- **Fresh disclosures on insurance business leads to lower value for life insurance business**
- **Maintain OP with a revised target price of Rs2,780; we recommend buying on declines**

Bajaj Auto reported 4Q net profit at Rs3.1 bn reflecting an 11% yoy decline but higher than our estimate of Rs2.7 bn. However, 4Q EBITDA at Rs3.3 bn was in-line with our estimate of Rs3.2 bn for the quarter. Higher-than-expected other income at Rs1.6 bn (our forecast Rs1.2 bn) led to the variation vis-'-vis our estimates. 4Q EBITDA margin at 14.1% declined 550 bps yoy and 10 bps qoq. We lower our EPS estimates for Bajaj Auto 6% for FY2008 to Rs130.3 (Rs138.0 previously) and 5% for FY2009 to Rs151.5 (160.3 previously) factoring in lower volume growth in both 2Ws and 3Ws over the period.

However, the highlight of the 4Q results was 1. Announcement of demerger of the company's auto and finance businesses; and 2. Disclosure by the company that Allianz – the foreign partner in the insurance ventures – has a call option to hike its stake to 74% (in case of life insurance) and 50% (in case of general insurance) from the current level of 26% at nominal valuations. Factoring in the above changes and announcements, we lower our SOTP target price for Bajaj Auto to Rs2,780 (Rs2,860 previously). We maintain our Outperform rating on the stock. We would recommend buying the stock if it sees a sharp decline today post the disclosures made yesterday.

Lowering volume and EPS estimates over FY2008-09

We lower our EPS estimates for Bajaj Auto 6% for FY2008 to Rs130.3 (Rs138.0 previously) and 5% for FY2009 to Rs151.5 (160.3 previously). Our revised estimates factor in the following changes:

Two-wheelers: We lower our motorcycle growth forecast for FY2008 to 10% in FY2008 (16% previously) and to 12% for FY2009 (16% previously). We now expect 7.5% domestic volume growth in motorcycles in FY2008 (15% previously) and 25% growth in motorcycle exports (unchanged). Bajaj Auto's domestic motorcycle sales dropped a steep 24% in April as it cut dispatches to dealers to alleviate rising inventories. We expect volumes to improve in coming months as the inventory problem will likely be more or less dealt with by May-end. Volumes will likely get a boost 3Q onwards as Bajaj Auto is planning to launch a new 125CC bike at the price point of 100CC bikes sometime in 2Q. Nevertheless with retail demand continuing to remain weak due to the sharp rise in interest rates, we lower our domestic volume growth forecast for Bajaj Auto for FY2008 to 7.5%. We expect better volume domestic growth in FY2009 at 10% as volumes of the new bike get ramped up.

Three-wheelers: We lower our total 3W volume growth forecast for FY2008 to 2% (9% previously) and maintain our FY2009 growth estimate at 10%. We now expect yoy volume declines in domestic sales for both goods and passenger 3Ws in FY2008. However, a strong 20% rise in 3W exports will likely keep 3W sales growth in positive territory for Bajaj Auto in FY2008. We note that the last few months have seen a sharp drop in industry goods 3W sales due to competition from Tata Motor's 'Ace' and M&M's 'Maxx' pick-up truck.

Margins: We forecast Bajaj Auto's EBITDA margins to remain subdued in 1HFY2008 at 14.2%. We expect margins to improve in 2HFY2008 to about 14.7% as volumes of Bajaj Auto's new 125CC bike start coming in. We expect margins of the new bike to be better than those of its existing 100CC bikes.

De-merger announcement will likely lead to unlocking of value

Bajaj Auto (BAL) has announced the much-anticipated demerger of the company's auto and finance businesses. The key highlights of the scheme of the de-merger are as given below:

a) Formation of two 100% subsidiaries:

1. Bajaj Holdings and Investment Limited (BHIL)
2. Bajaj Finserv Limited (BFL)

b) BAL will subscribe to shares of BHIL (43.5 mn shares of face value Rs10) and BFL (43.5 mn shares of face value Rs5). We understand that these shares will be allotted at par value.

c) The entire auto business with relevant assets and liabilities along with investments in Indonesia and few vendor companies will be transferred to BHIL. In addition, Rs15 bn of cash and cash equivalents will also be transferred to BHIL

d) The wind power project, investments in the insurance subsidiaries and the investment in Bajaj Auto Finance along with relevant assets and liabilities will be transferred to BFL. In addition, Rs8 bn of cash and cash equivalents will also be transferred to BFL.

e) Balance assets and liabilities including balance cash and cash equivalents amounting to about Rs60 bn (market value) will remain in BAL. The two new companies will be able to access these funds on an arms-length basis to support future growth initiatives.

f) BHIL will be renamed Bajaj Auto Limited and BAL will be renamed Bajaj Holding and Investment Limited

g) All existing shareholders of Bajaj Auto will be issued shares in the two new companies in the ratio 1:1

Fresh disclosures on insurance businesses leads to lower value for life insurance business

Based on disclosures made by Bajaj Auto's management, Allianz SE has the option to increase its stake in Bajaj Allianz Life Insurance to 74% from current 26%. This agreement will likely hold till 30th July 2016 and is subject to the government increasing FDI limit to 74%.

In case Allianz manages to exercise this option prior to the specified dates (30th July 2016), Bajaj Auto will get a price of Rs5.42 per share plus interest at 16% compounded per annum for the 48% transferred to Allianz. If this option is exercised post 30th July 2016 Bajaj Auto Ltd will likely benefit and get a higher price i.e market price in case the company is listed or fair value as determined by mutually accepted accounting firm.

We believe that the government is in favor of increasing the FDI limit to 49% but the possibility of this going to 74% appears very unlikely at this stage. We are accordingly giving Bajaj Auto credit for 38% (between 26% and 50%) stake for now and assign a value of Rs467 per share. In case the holding is less at 26%, our value per share assigned to Bajaj Auto will fall to Rs319. Our Banking and Insurance analyst – Tabassum Inamdar values the company using the appraisal value method. We estimate Bajaj Allianz premium income to grow by 66% in FY2008 to Rs53bn and 49% to Rs79bn in FY2009. Given the higher proportion of single premium income and lower persistency ratio we assume margin of 8.8% for Bajaj Allianz as against 13.5% for ICICI Prudential Life and use a 17X multiple on new business value. The company does not declare its margins and we believe this could carry risk of downside. We also apply a 15% holding company discount

Effective stake in Bajaj Allianz General Insurance is 50%

As is the case with Bajaj Allianz Life Insurance Ltd, Allianz management has the option to increase its stake in Bajaj Allianz General Insurance to around 50% from 26% currently. This agreement will hold till 22nd April 2016 and is subject to the government increasing FDI limits to 50%.

In case Allianz manages to exercise this option prior to the specified dates, Bajaj Auto Ltd will get a price of Rs10 per share plus interest at 16% compounded per annum for the 24% transferred to Allianz. If this option is exercised post 23 April 2016 Bajaj Auto Ltd will likely benefit and get a higher price i.e market price in case the company is listed or fair value as determined by mutually accepted accounting firm.

We have valued Bajaj Allianz General Insurance at 6X FY2007 BVPS. General insurance companies generally trade at 1.5-2X P/B. However, given the strong growth in premium collection in India we believe that the general insurance business will likely trade at higher valuations. At 50% holding, this amounts to Rs102 per share, after giving a 15% holding company discount.

Revised SOTP target price if Rs2,780; maintain Outperform on the stock

Our revised target price for Bajaj Auto is Rs2,780. This comprises of the following:

Core business value - Rs1,861: This is based on 7X FY2009 EV/EBITDA equivalent to 12.8X FY2009 P/E. Our previous value for the core business was Rs1,939 based on 8.5X FY2008 EV/EBITDA. We lower our target multiple taking into account rising risks to industry volume growth due to the sharp rise in interest rates and the worsened level of competition between Hero Honda and Bajaj Auto.

Note that this value includes the non-equity part of the investment book, which gets accounted for in the net debt calculations as part of enterprise value.

Bajaj Allianz Life Insurance – Rs467 per share: This is based on a 17X new business multiple assuming 8.8% margin on FY2009 basis. This gives Bajaj credit for 38% holding as explained above.

Bajaj Allianz Life Insurance – Rs102 per share: This is based on a 6X FY2007 P/B. This gives Bajaj credit for 50% holding as explained above.

Listed equity investments – Rs350 per share: This is based on market value of holding less a 10% holding company discount. We lower our discount to 10% (20% previously) as in our opinion, the demerger scenario justifies a lower discount. The stake in ICICI Bank amounts to Rs308 of this value.

Our revised target price provides 11% upside to current stock price. We recommend buying the stock if it sees a sharp fall today due to an over-reaction to the disclosures made regarding the insurance subsidiaries. Bajaj Auto remains our preferred two-wheeler play. We see upside risk to our EPS estimates for the company if the new 125CC launch in 2Q succeeds in pulling away a meaningful number of Hero Honda's customers. We maintain our Outperform rating on the stock.

Bajaj Auto: 4QFY2007 results

(in Rs mn)	4QFY06	3QFY07	4QFY07	% chg. qoq	% chg. yoy	Kotak estimates 4QFY07	% deviation	FY06	FY07	% chg.
Net sales	**21,659**	**25,682**	**23,136**	**(9.9)**	**6.8**	**21,804**	**6.1**	**76,643**	**95,204**	**24.2**
Operating costs	**(17,409)**	**(22,046)**	**(19,873)**	**(9.9)**	**14.2**	**(18,640)**	**6.6**	**(63,116)**	**(81,034)**	**28.4**
(Inc/Dec in Stock)	430	47	237	405.6	(45.0)	(258)	(191.8)	(619)	(9)	(98.5)
Raw Materials	(15,291)	(18,903)	(17,155)	(9.2)	12.2	(14,907)	15.1	(51,314)	(69,001)	34.5
Staff Cost	(682)	(757)	(688)	(9.1)	0.9	(746)	(7.8)	(2,741)	(3,015)	10.0
Other Expenditure	(1,866)	(2,433)	(2,266)	(6.9)	21.4	(2,729)	(17.0)	(8,442)	(9,009)	6.7
EBITDA	**4,250**	**3,636**	**3,263**	**(10.3)**	**(23.2)**	**3,164**	**3.1**	**13,527**	**14,170**	**4.8**
Other income	1,031	1,610	1,577	(2.0)	53.0	1,171	34.6	4,420	5,556	25.7
Interest costs	1	(2)	(24)	986.4	(4,083.3)	1		(3)	(53)	1,470.6
Depreciation	(468)	(472)	(458)	(3.1)	(2.2)	(526)	(13.1)	(1,910)	(1,903)	(0.4)
Extraordinairies	133	(120)	(124)	4.1	(193.3)	(138)		(226)	(498)	120.1
PBT	**4,947**	**4,652**	**4,234**	**(9.0)**	**(14.4)**	**3,672**	**15.3**	**15,807**	**17,272**	**9.3**
Taxes	(1,476)	(1,200)	(1,151)	(4.1)	(22.0)	(1,000)	15.1	(4,791)	(4,901)	2.3
PAT	**3,471**	**3,452**	**3,083**	**(10.7)**	**(11.2)**	**2,672**	**15.4**	**11,016**	**12,371**	**12.3**
Key ratios										
Volumes	619,549	738,219	625,588	(15.3)	1.0	625,588		2,280,995	2,719,026	19.2
Net realizations (Rs/vehicle)	34,959	34,790	36,982	6.3	5.8	34,853		33,601	35,014	4.2
RM/Net sales (%)	68.6	73.4	73.1	(0.3)	4.5	69.5		67.8	72.5	4.7
RM/VOP (%)	69.2	73.5	73.4	(0.1)	4.2	69.2		67.5	72.5	5.0
EBITDA per vehicle (Rs)	6,860	4,926	5,216	5.9	(24.0)	5,058		5,930	5,211	(12.1)
EBITDA margin (%)	19.6	14.2	14.1	(0.1)	(5.5)	14.5		17.6	14.9	(2.8)
PAT margin (%)	16.0	13.4	13.3	(0.1)	(2.7)	12.3		14.4	13.0	(1.4)
Effective tax rate (%)	29.8	25.8	27.2	1.4	(2.7)	27.2		30.3	28.4	(1.9)

Source: Company data, Kotak Institutional Equities

Our SOTP target price for Bajaj Auto is Rs2,780

Value of core business at 7X FY2009 EV/EBITDA equivalent to 12.5X FY2009 P/E	1,861
Value of Bajaj Allianz General Insurance at 6X FY2007 BVPS	102
Value of Bajaj Allianz Life Insurance (17X NBAL on FY2009 basis at 38% holding)	467
Value of stake in ICICI Bank (at 10% discount to market value)	308
Value of other listed investments (at 10% discount to market value)	42
SOTP based target price	**2,780**

Source: Kotak Institutional Equities

Volume assumptions for Bajaj Auto

	2005	2006	2007	2008E	2009E
Volumes (units)					
Motorcycles-domestic	1,325,727	1,747,289	2,079,274	2,235,219	2,458,741
Motorcycles-exports	123,950	165,288	297,518	371,898	464,873
Total motorcycles	**1,449,677**	**1,912,577**	**2,376,792**	**2,607,117**	**2,923,614**
Geared scooters	102,575	62,860	5,254	-	-
Ungeared scooters	30,931	52,612	15,257	30,515	33,566
Step-thrus	19,165	870	-	-	-
Total two-wheelers	**1,602,348**	**2,028,919**	**2,397,304**	**2,637,632**	**2,957,180**
Passenger three-wheelers-domestic	123,794	141,351	138,524	124,672	124,672
Goods three-wheelers-domestic	32,446	35,394	41,411	33,129	33,129
Three-wheeler exports	65,747	75,261	141,788	170,145	204,174
Total three-wheelers	**221,987**	**252,006**	**321,722**	**327,945**	**361,974**
Total vehicles	**1,824,335**	**2,280,925**	**2,719,026**	**2,965,578**	**3,319,155**
YoY growth (%)					
Motorcycles-domestic	40.9	31.8	19.0	7.5	10.0
Motorcycles-exports	49.6	33.4	80.0	25.0	25.0
Total motorcycles	**41.6**	**31.9**	**24.3**	**9.7**	**12.1**
Geared scooters	(42.4)	(38.7)	(91.6)	(100.0)	-
Ungeared scooters	(43.5)	70.1	(71.0)	100.0	10.0
Step-thrus	(41.0)	(95.5)	(100.0)	-	-
Total two-wheelers	**24.3**	**26.6**	**18.2**	**10.0**	**12.1**
Passenger three-wheelers-domestic	(10.7)	14.2	(2.0)	(10.0)	-
Goods three-wheelers-domestic	31.0	9.1	17.0	(20.0)	-
Three-wheeler exports	(0.1)	14.5	88.4	20.0	20.0
Total three-wheelers	**(3.1)**	**13.5**	**27.7**	**1.9**	**10.4**
Total vehicles	**20.2**	**25.0**	**19.2**	**9.1**	**11.9**

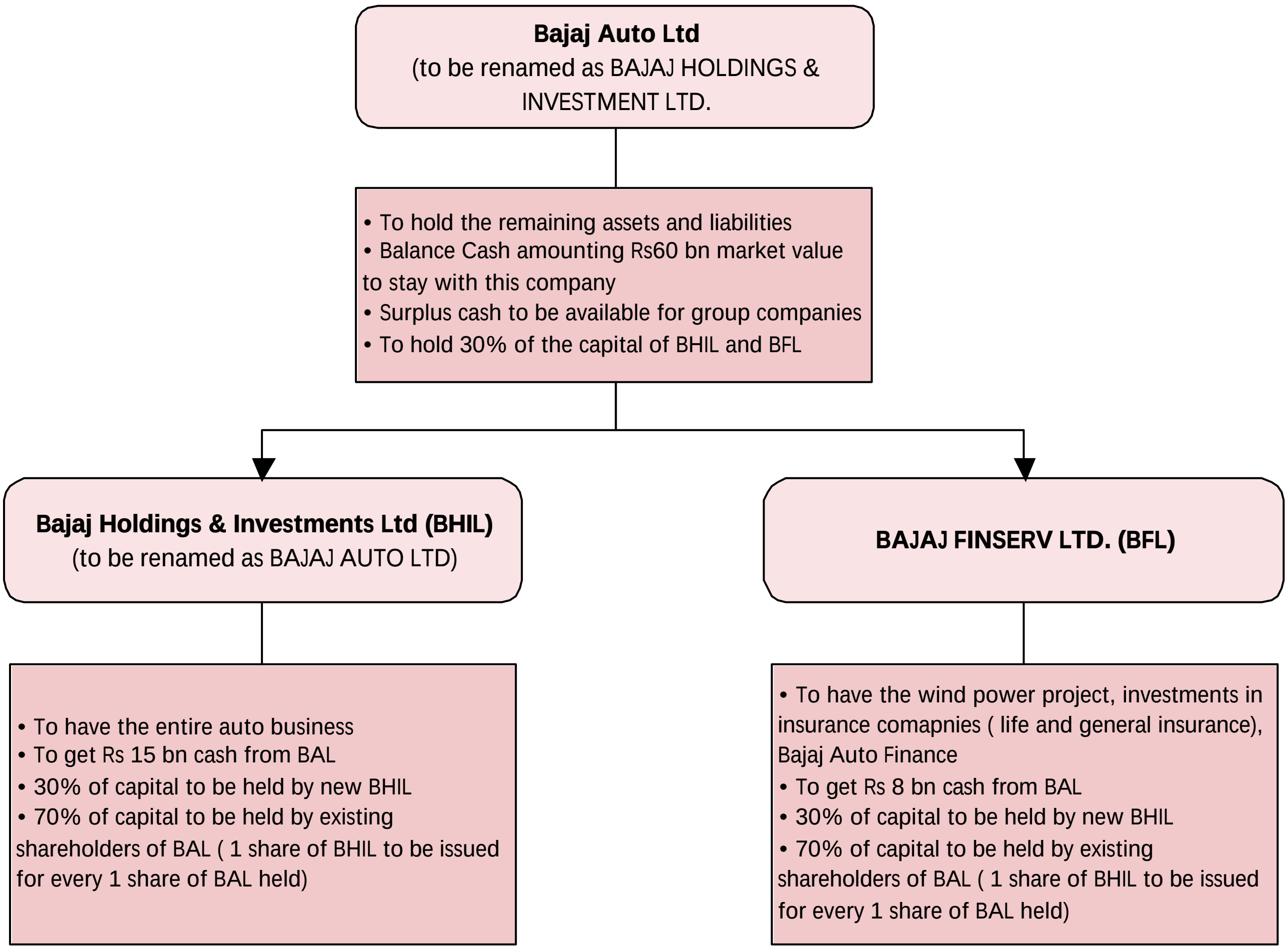
Source: SIAM, Kotak Institutional Equities estimates

Financial Snapshot for Bajaj Auto

YE March 31, in Rs mn	2005	2006	2007	2008E	2009E
Profit & Loss Account (Rs mn)					
Net sales	57,613	74,893	93,873	104,415	119,997
EBITDA	7,476	11,777	14,060	15,094	17,914
Other Income	5,739	6,170	5,151	5,510	5,735
Interest	(7)	(3)	(28)	(56)	(56)
Depreciation	(1,854)	(1,910)	(1,971)	(2,214)	(2,538)
PBT	11,355	16,034	17,211	18,334	21,055
Extraordinaries	(867)	(226)	(500)	(500)	(500)
Taxes	(3,196)	(4,791)	(4,750)	(4,654)	(5,228)
PAT	7,292	11,016	11,961	13,179	15,327
EPS (Fully diluted, Rs per share)	**72.1**	**108.9**	**118.2**	**130.3**	**151.5**
Balance Sheet (Rs mn)					
Equity capital	1,012	1,012	1,012	1,012	1,012
Reserves & surplus	41,731	47,571	54,897	62,409	71,035
Total borrowings	12,270	14,672	15,171	15,171	15,171
Total Liabilities	**55,012**	**63,255**	**71,080**	**78,592**	**87,218**
Total fixed assets	11,408	11,558	9,585	15,121	17,582
Cash	1,087	821	1,112	2,990	4,471
Net working capital (excl. cash)	(3,129)	(7,708)	(12,180)	(14,564)	(17,483)
Other long term assets	45,646	58,583	72,563	75,046	82,648
Total Assets	**55,012**	**63,255**	**71,080**	**78,592**	**87,218**
Cash Flow (Rs mn)					
Operating cash flow (excl. working capital)	4,869	7,665	10,137	11,282	13,575
Working capital changes	(395)	4,579	4,472	2,384	2,920
Capital expenditure	(407)	(1,651)	2	(7,750)	(5,000)
Other income	3,913	4,292	3,795	4,112	4,290
Free cash flow	**7,980**	**14,884**	**18,406**	**10,027**	**15,785**
Ratios (%)					
Sales growth	20.5	30.0	25.3	11.2	14.9
Ebitda growth	4.2	57.5	19.4	7.4	18.7
EPS growth	(1.2)	51.1	8.6	10.2	16.3
Ebitda margin	13.0	15.7	15.0	14.5	14.9
Debt/ Equity (X)	0.3	0.3	0.3	0.2	0.2
RoAE	19.4	24.4	23.5	22.6	23.1
RoACE	22.0	27.2	25.7	24.6	25.5

Source: Company, Kotak Institutional Equities estimates

Scheme of demerger



Note
(1) Each existing shareholder of Bajaj Auto Ltd would get 1 share each of BAL, BHIL and BFL upon demerger
(2) Existing BAL (to be later renamed as Bajaj Holdings & Investments Ltd) would subscribe to 30% of the equity of BHIL and BFL at face value

Source: Company

We value stake in Bajaj Allianz Life Insurance at Rs467 per share at 38% holding

Contribution to sum-of-parts assuming full value for 50% (Rs per share)

	Margin (%)					
Multiple (X)	**4.9**	**6.8**	**8.8**	**10.8**	**12.8**	**14.7**
14	342	434	526	618	710	802
16	375	480	585	690	795	900
17	391	503	**614**	726	838	949
18	407	525	644	762	880	998
20	440	571	702	834	965	1,097

Contribution to sum-of-parts assuming full value for 38% (Rs per share)

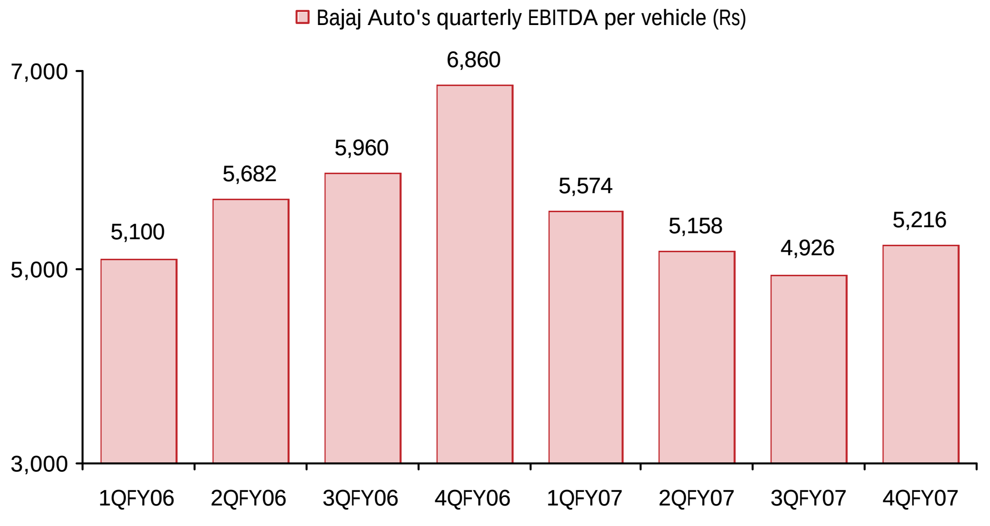
Multiple (X)	**4.9**	**6.8**	**8.8**	**10.8**	**12.8**	**14.7**
14	260	330	400	470	540	610
16	285	365	445	524	604	684
17	297	382	**467**	552	637	721
18	309	399	489	579	669	759
20	334	434	534	634	733	833

Contribution to sum-of-parts assuming full value for 26% (Rs per share)

Multiple (X)	**4.9**	**6.8**	**8.8**	**10.8**	**12.8**	**14.7**
14	178	226	274	321	369	417
16	195	250	304	359	413	468
17	203	261	**319**	378	436	494
18	212	273	335	396	458	519
20	229	297	365	434	502	570

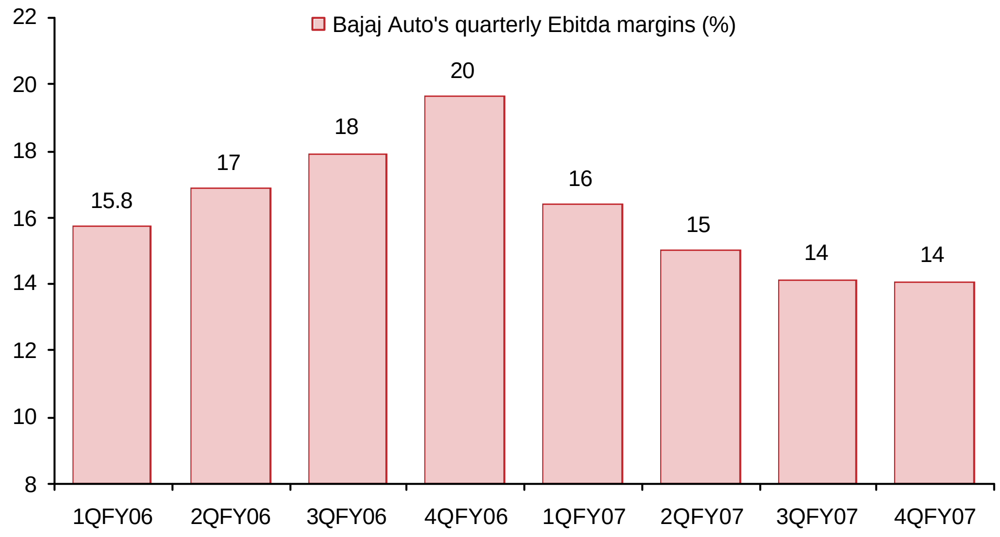
Source: Kotak Institutional Equities

Bajaj Auto's EBITDA per vehicle has improved in 4Q



Source: Kotak Institutional Equities

Bajaj Auto's EBITDA margins have fallen sharply in FY2007



Source: Kotak Institutional Equities

Diversified

MAXI.BO, Rs259	
Rating	IL
Sector coverage view	-
Target Price (Rs)	220
52W High -Low (Rs)	264 - 102
Market Cap (Rs bn)	46.6

Financials

March y/e	2007	2008E	2009E
Sales (Rs bn)	1.7	2.8	3.3
Net Profit (Rs bn)	0.1	0.1	0.1
EPS (Rs)	0.5	0.7	0.4
EPS gth	*51.3*	*39.0*	*(40.3)*
P/E (x)	504.5	363.0	608.2
EV/EBITDA (x)	1,419	390.5	243.7
Div yield (%)	-	-	-

Shareholding, March 2007

	Pattern	% of Portfolio	Over/(under) weight
Promoters	39.0	-	-
FIIs	18.6	0.3	(0.0)
MFs	9.2	0.9	0.6
UTI	-	-	(0.4)
LIC	7.9	0.7	0.4

Max India: Insurance is the key driver; stock seems expensive

Pawan Nahar : pawan.nahar@kotak.com, +91-22-6634-1461
Tabassum Inamdar : tabassum.inamdar@kotak.com, +91-22-6634-1252

- **Life Insurance premium growth lower than full year estimates**
- **Equity issuance planned for investments into insurance business**
- **Portfolio of long gestation businesses imply losses till FY2010**
- **Our SOTP price target is Rs220; rolled over to FY2009; maintain IL rating**

Max New York Life premium income growth for FY2007 is 81% (45-50% growth in Q4). This falls short of our full year estimate of a 93% growth in premium income for FY2007. We have modeled 50% growth in premium income in FY2008 and 40% in FY2009. We have valued Max India's investment in Max New York Life (50% stake assumed) at Rs154/ share, rolled over to FY2009 estimates. Healthcare revenues were on track, growth of 79% yoy. We have valued investment in Max Healthcare to Rs46/share. We have rolled over to FY2009 SOTP based price target of Rs220/share (Rs165/share earlier); see Exhibit 1. The stock seems expensive; particularly after the 21% rise in the last two trading sessions. Maintain IL rating.

Portfolio of long gestation businesses imply losses till FY2010

On a SOTP basis, we value Max India at Rs200/share – see Exhibit 1. Max India, through its subsidiaries has invested into life insurance and healthcare business. The group's new business initiatives focus on life and population, and are a part of the service industry. The third business, which holds potential is the healthcare staffing business, but very nascent at this moment. Other businesses include clinical trials and manufacturing of specialty plastics. We expect both the insurance and healthcare business to make losses till FY2010. The standalone numbers reflect the financials of Max India, which hosts the manufacturing business of plastic films (used for packaging) and investment income.

Premium growth lower than estimates: Max New York Life Insurance (MNYL) reported adjusted first year premium (AFYP) income of Rs9.7bn, 81% growth yoy in FY2007. MNYL premium income growth in the 4QFY07 was likely lower at around 45-50%. MNYL market share in individual business slipped marginally to 1.9% in FY2007 from 2.1% in FY2006. As mentioned in our previous note MNYL growth rate has fallen short of our full year growth estimate of 93% in AFYP in FY2007.

Despite the slowdown in the 4QFY07, we are assuming MNYL will grow its adjusted premium income by 50% in FY2008 and 40% in FY2009. MNYL has expanded its agency force by 64% in FY2007, the benefits of which will likely accrue in the year ahead. Given the increasing competition we expect the company to increase its investments in the insurance business over the next two years to around Rs3bn each in FY2008 and FY2009.

We are rolling over our fair value estimate for the insurance business to FY2009, which now stands at Rs154 per share of Max India Ltd (before holding company discount). We assume a blended margin of 13.9% for the purpose of calculating the new business value. We assume that Max India economic value in the JV will be restricted to 50%.

Equity issuance planned for investments into insurance business. Max India has plans to raise equity of upto Rs10 bn, by issue of equity to Qualified Institutional Buyers (QIBs) in one or more tranches. We believe that the SEBI formula for the issue price is about Rs230/share. This money we believe will be largely used for additional investments into the life-insurance business and also for maintaining a war chest.

Healthcare revenues will likely grow by 42% in FY2008. Max Healthcare ended FY2007 with revenues of Rs2.45 bn, growth of 79%. Its network includes 5 hospitals and about 620 operating beds. Occupancy was 63.5%, on average occupational beds. We note that two large hospitals are under management contracts, thus the reported revenue would be lower than the above. The company in all investor presentations mentions revenue numbers, including of these two management contracts.

We estimate the operational bed count will rise to 669 in FY2008 and 875 in FY2009. We have modeled revenues of Rs3.5 bn in FY2008 and Rs4.4 bn in FY2009. We estimate EBITDA margins of –0.6% in FY2007, 3% in FY2008 and 13% in FY2009. While, in the short to medium term margins are impacted by the gestation period of new hospitals. At mature stage, we expect EBITDA margin of 25%.

Max India has an option to invest an additional Rs534 mn in Max Healthcare at Rs10/share. In FY2007, Max India invested Rs216 mn in Max Healthcare. In total, it has an option to invest upto Rs750 mn. We have assumed that the balance will be invested in FY2008. We note that this investment will be made at face value (Rs10), thereby resulting in fully diluted equity of 281 mn shares. Our valuations are based on the fully diluted equity.

We are rolling forward our DCF to March 2009 and our equity value of the hospital business is Rs10.7 bn. On an EV basis (Rs14.4 bn), it implies a multiple of 18X on FY2009 EBITDA and 2.9X book value. Accordingly, we value Max India's 78% stake in Max Healthcare at Rs46/share.

Other businesses

Health staffing business set for strong growth. Max HealthStaff is a staffing company, which trains nurses and helps them with overseas placements. 55 nurses were placed in the US in FY2007 and another 200-300 in FY2008. The pipeline comprises 600 nurses at different stages of the program. Typically, 18 months is the lead-time for training and visa processing. While this venture is still in its infancy, it seems well placed to benefit from the current shortage of nurses, in markets like the US, EU and Middle East.

Order book in clinical research is rising. Clinical research services are offered through Neeman Medical (and its subsidiaries) at sites in India, Latin America and the United States. In the past three years, costs have exceeded revenues, thus resulting in accumulated losses. The company has repositioned itself as a contract research organization from a site management company earlier. It is now focusing on operating out of India and has also increased its service offerings. Client base has increased from 14 to 29. In FY2006, the clinical trial business made a loss of Rs171 mn on a turnover of Rs86 mn. We have not attributed any value to this business till we see signs of a turnaround.

Specialty products are growing strongly. Max India is also into manufacturing plastic products, mainly used in the packaging industry, through Max Speciality Products. This is the traditional business and forms part of the listed company. The company has commissioned its third metalliser (a new production line), and this should help drive future growth. For FY2007, segment sales were Rs1.55 bn and EBITDA margin of 10%. However, as Max India also hosts the group corporate office, the reported margins have come down over the past three years; to 2% in FY2007 from 13% in FY2004, impacted by the rise in corporate overheads. We think Max India will continue to report minimal EBITDA for some time.

Key risks

In the insurance business, lower-than-expected premium income growth and margins are a risk. In the healthcare business, lower occupancy and delays in new facility launches are risks. Another important risk is termination of service agreements, or unfavourable regulations on trust-owned hospitals, which could materially impact estimates.

We value Max India at Rs220/share
Sum-of-parts valuation

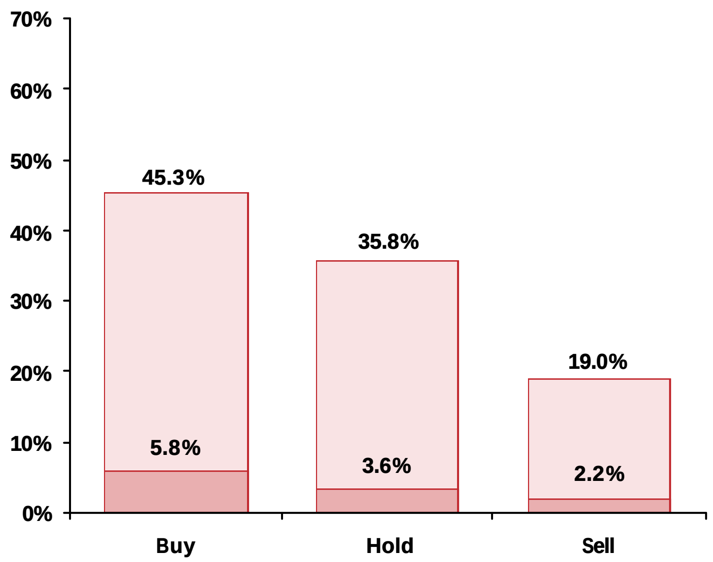
Company	Equity Value (Rs mn)	Stake (%)	Value of stake (Rs mn)	Per-Share Value (Rs)	Investment by Max India	Valuation methodology	Comments
Max New York Life Insurance	55,564	50	27,782	**154**	4,920	Appraisal value	Adjusted for the 24% stake, investment for which is being reimbursed by NewYork Life
Max Healthcare Institute	10,669	78	8,322	**46**	2,195	NPV	We have assumed that stake of Max India will rise to 78% (from 73%), by infusing Rs535 mn at Rs10/share.
Plastic films/Max India	2,661	100	2,661	**15**	1,150	NPV	Specialty plastics is part of listed company, which also bears corporate overheads.
Max Healthstaff	2,440	100	2,440	**14**	45	PE	Valued at 20X earnings potential of likely placements in FY2008
Neeman (clinical trials)		100			928		We are not attributing any value, till we see signs of turnaround
Less: Holding company discount			(1925)	(11)			Assuming a 5% discount on value of subsidiaries
Total	**71,334**		**39,280**	**218**	**9,237**		

	Q4FY06	Q1FY07	Q2FY07	Q3FY07	Q4FY07	FY2006	FY2007	FY2008E
Net Sales	**322**	**316**	**396**	400	442	**1245**	1553	2608
Total Expenditure	338	329	417	411	489	1296	1646	2694
- Material cost	205	203	277	273	293	775	1045	1625
- Staff cost	48	38	53	55	86	165	232	468
- Other exp	85	89	87	83	110	356	369	601
EBITDA	**(17)**	**(13)**	**(21)**	**(11)**	**(47)**	**(52)**	**(93)**	**(86)**
Other operating income	23	33	30	26	36	96	125	210
Depreication	15	15	14	12	17	62	58	104
EBIT	(9)	5	(5)	3	(29)	(17)	(25)	20
Interest	12	15	11	11	12	95	49	87
Income from investment activities	65	65	58	56	50	148	229	210
PBT	**45**	**55**	**42**	**48**	**9**	**35**	**154**	**143**
Current Tax	1	5	0	2	(3)	4	4	14
Deferred Tax	(4)			7	51	(28)	58	0
Exceptional charges		(50)					(50)	0
Rep. PAT	48	100	42	39	(38)	59	142	128
Adj. PAT	**48**	**50**	**42**	**39**	**(38)**	**59**	**92**	**128**
Operating ratios (%)								
- Material cost	63.9	64.2	69.9	68.3	66.3	62.3	67.3	62.3
- Staff cost	15.0	12.0	13.5	13.6	19.5	13.2	14.9	17.9
- Other exp	26.4	28.0	21.9	20.8	24.9	28.6	23.7	23.1
- EBITDA margin	(5.3)	(4.2)	(5.3)	(2.7)	(10.7)	(4.2)	(6.0)	(3.3)
- Net margin	14.8	15.8	10.6	9.6	(8.6)	4.7	5.9	4.9

"Each of the analysts named below hereby certifies that, with respect to each subject company and its securities for which the analyst is responsible in this report, (1) all of the views expressed in this report accurately reflect his or her personal views about the subject companies and securities, and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report: Abhijeet Naik, Pawan Nahar."

Kotak Institutional Equities Research coverage universe

Distribution of ratings/investment banking relationships



Percentage of companies covered by Kotak Institutional Equities, within the specified category.

Percentage of companies within each category for which Kotak Institutional Equities and or its affiliates has provided investment banking services within the previous 12 months.

* The above categories are defined as follows: Buy = OP; Hold = IL; Sell = U. Buy, Hold and Sell are not defined Kotak Institutional Equities ratings and should not be constructed as investment opinions. Rather, these ratings are used illustratively to comply with applicable regulations. As of 03/31/07 Kotak Institutional Equities Investment Research had investment ratings on 137 equity securities.

Source: Kotak Institutional Equities. As of March 31, 2007

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.

Our target price are also on 12-month horizon basis.

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).

Other ratings/identifiers

NR = Not Rated. The investment rating and target price, if any, have been suspended temporarily. Such suspension is in compliance with applicable regulation(s) and/or Kotak Securities policies in circumstances when Kotak Securities or its affiliates is acting in an advisory capacity in a merger or strategic transaction involving this company and in certain other circumstances.
CS = Coverage Suspended. Kotak Securities has suspended coverage of this company.
NC = Not Covered. Kotak Securities does not cover this company.
RS = Rating Suspended. Kotak Securities Research has suspended the investment rating and price target, if any, for this stock, because there is not a sufficient fundamental basis for determining an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.
NA = Not Available or Not Applicable. The information is not available for display or is not applicable.
NM = Not Meaningful. The information is not meaningful and is therefore excluded.

Corporate Office
Kotak Securities Ltd.
Bakhtawar, 1st Floor
229, Nariman Point
Mumbai 400 021, India
Tel: +91-22-6634-1100

Overseas Offices

Kotak Mahindra (UK) Ltd.
6th Floor, Portsoken House
155-157 The Minories
London EC 3N 1 LS
Tel: +44-20-7977-6900 / 6940

Kotak Mahindra Inc.
50 Main Street, Suite No.310
Westchester Financial Centre
White Plains, New York 10606
Tel: +1-914-997-6120

Kotak Securities Limited and its affiliates are a full-service, integrated investment banking, investment management, brokerage and financing group. We along with our affiliates are leading underwriter of securities and participants in virtually all securities trading markets in India. We and our affiliates have investment banking and other business relationships with a significant percentage of the companies covered by our Investment Research Department. Our research professionals provide important input into our investment banking and other business selection processes. Investors should assume that Kotak Securities Limited and/or its affiliates are seeking or will seek investment banking or other business from the company or companies that are the subject of this material and that the research professionals who were involved in preparing this material may participate in the solicitation of such business. Our research professionals are paid in part based on the profitability of Kotak Securities Limited, which include earnings from investment banking and other business. Kotak Securities Limited generally prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, Kotak Securities Limited generally prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover. Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein.

This material should not be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. We are not soliciting any action based on this material. It is for the general information of clients of Kotak Securities Limited. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, clients should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice. The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur. Kotak Securities Limited does not provide tax advise to its clients, and all investors are strongly advised to consult with their tax advisers regarding any potential investment.

Certain transactions -including those involving futures, options, and other derivatives as well as non-investment-grade securities - give rise to substantial risk and are not suitable for all investors. The material is based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied on as such. Opinions expressed are our current opinions as of the date appearing on this material only. We endeavor to update on a reasonable basis the information discussed in this material, but regulatory, compliance, or other reasons may prevent us from doing so. We and our affiliates, officers, directors, and employees, including persons involved in the preparation or issuance of this material, may from time to time have “long” or “short” positions in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. For the purpose of calculating whether Kotak Securities Limited and its affiliates holds beneficially owns or controls, including the right to vote for directors, 1% of more of the equity shares of the subject issuer of a research report, the holdings does not include accounts managed by Kotak Mahindra Mutual Fund.Kotak Securities Limited and its non US affiliates may, to the extent permissible under applicable laws, have acted on or used this research to the extent that it relates to non US issuers, prior to or immediately following its publication. Foreign currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of or income derived from the investment. In addition , investors in securities such as ADRs, the value of which are influenced by foreign currencies affectively assume currency risk. In addition options involve risks and are not suitable for all investors. Please ensure that you have read and understood the current derivatives risk disclosure document before entering into any derivative transactions.

This report has not been prepared by Kotak Mahindra Inc. (KMInc). However KMInc has reviewed the report and, in so far as it includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed. Any reference to Kotak Securities Limited shall also be deemed to mean and include Kotak Mahindra Inc.