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### News Roundup

#### Corporate

- Reviving the possibility of a merger with Idea Cellular, Spice Communication's Chairman, BK Modi, said he was in talks with the Aditya Birla Group to explore merging the two entities. The two companies had initially begun discussions a year ago but the deal could not be closed due to issues related to valuation. (BL)
- Punj Lloyd Group, a specialist in engineering, procurement and construction services, has acquired a strategic 74% stake in Technodyne International Limited, UK for an undisclosed amount. (BS)
- Hyderabad-based GMR Industries Ltd, the agri-business division of GMR Group, is investing close to Rs 8 bn to set up sugar mills in Karnataka. (BS)

#### Economic and political

- Corporate houses and investors will be able to trade in currency futures at exchanges in three months. Capital market regulator Securities & Exchange Board of India said it was working with the Reserve Bank of India to help companies and investors hedge their currency risks by introducing exchange-traded currency futures. (ET)
- Soon, companies listed on the domestic bourses will not have to file a separate prospectus to list on stock markets abroad. Securities market regulators across the world are working on evolving common standards that minimize the need for registration in every country, Sebi chairman CB Bhavé said. (FE)

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

### EQUITY MARKETS

	Change, %			
	3-Jun	1-day	1-mo	3-mo
<b>India</b>				
Sensex	15,963	(0.6)	(9.3)	(2.3)
Nifty	4,716	(0.5)	(9.8)	(3.1)
<b>Global/Regional indices</b>				
Dow Jones	12,403	(0.8)	(5.0)	1.5
Nasdaq Composite	2,480	(0.4)	0.1	9.7
FTSE	6,058	0.8	(2.5)	5.0
Nikkei	14,381	1.2	2.4	10.7
Hang Seng	24,328	(0.2)	(7.3)	5.2
KOSPI	1,822	0.2	(1.4)	8.7
<b>Value traded - India</b>				
		Moving avg, Rs bn		
	3-Jun	1-mo	3-mo	
Cash (NSE+BSE)	176.6	198.9	194.5	
Derivatives (NSE)	352.6	363.0	491	
Deri. open interest	648.2	676	637	

#### Forex/money market

	Change, basis points			
	3-Jun	1-day	1-mo	3-mo
Rs/US\$	42.5	0	186	223
6mo fwd prem, %	0.7	(25)	71	24
10yr govt bond, %	8.2	1	21	61

#### Net investment (US\$m)

	2-Jun	MTD	CYTD
FIs	(87)	-	(3,485)
MFs	(37)	-	1,367

#### Top movers -3mo basis

	Change, %			
	3-Jun	1-day	1-mo	3-mo
<b>Best performers</b>				
Chambal Fert	84	0.1	18.4	56.5
Infosys	1,922	(1.5)	7.5	35.5
Thomas Cook	102	(0.1)	1.9	27.5
i-Flex	1,325	(1.5)	(6.9)	26.4
Dr Reddy's	695	(3.5)	9.2	24.5
<b>Worst performers</b>				
Thermax	416	(2.6)	(16.8)	(36.8)
SAIL	156	1.5	(14.9)	(32.0)
Siemens India	540	(2.3)	(6.6)	(27.7)
Reliance Cap	1,116	(1.7)	(27.6)	(26.6)
BHEL	1,550	(2.8)	(18.8)	(26.1)

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**Banking****JKBK.BO, Rs649**

Rating	ADD
Sector coverage view	Attractive
Target Price (Rs)	750
52W High -Low (Rs)	1005 - 570
Market Cap (Rs bn)	31.5

**Financials**

March y/e	2008	2009E	2010E
Sales (Rs bn)	10.8	11.5	13.6
Net Profit (Rs bn)	3.6	3.6	3.7
EPS (Rs)	74.2	74.7	76.3
EPS <i>gth</i>	31.2	0.6	2.1
P/E (x)	8.7	8.7	8.5
P/B (x)	1.5	1.3	1.2
Div yield (%)	2.3	2.3	2.4

**Shareholding, March 2008**

	% of Pattern Portfolio	Over/(under) weight
Promoters	53.2	-
FIs	33.6	0.1
MFs	1.8	(0.0)
UTI	-	(0.1)
LIC	-	(0.1)

**J&K Bank: Profit better-than-expected, operational performance a mixed bag, retain ADD**

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- **J&K Bank reports PAT of Rs598 mn, a growth of 32% yoy and 16% ahead of estimates**
- **Operational performance a mixed bag—strong NII growth, while fee income growth disappoints**
- **Retain ADD rating with a slightly reduced target price of Rs750**

**Profit better-than-expected, operational performance a mixed bag, retain ADD**

Jammu and Kashmir Bank (J&K Bank) reported a PAT of Rs598 mn, a growth of 32% yoy and 16% ahead of our estimates. Healthy net interest income (NII) growth of 11% yoy, strong non-NII revenues aided by treasury profits, lower-than-expected employee expenses (reasons remain unclear), depreciation losses on the equity book and higher tax burden for meeting prior period expenses are the key highlights of the quarter. We have marginally modified our earnings estimates for FY2009 upwards by 3% for FY2009 and downwards by 11% for FY2010 (factoring in lower loan growth and slower fee income growth). We retain our ADD rating on the stock and marginally reduce our target price to Rs750 (previously Rs785).

**NII growth marginally above expectations**

- J&K Bank's NII in 4QFY08 was Rs2.2 bn (11% yoy growth), beating our estimates by 4%.
- The growth in this income stream, adjusted for the extraordinary income on CRR balances in 4QFY07, was 15% yoy.
- This income was driven by an improvement in NIM to 3.18% from 2.98% in 3QFY08 and was also aided by healthy loan book growth. The management indicated that the average loan growth (based on fortnightly averages) in the current quarter was 28% yoy as against the 11% yoy growth reported based on the period end figures. While we are happy to see this performance in 4QFY08, J&K Bank needs to maintain this trend. In the past, we have observed an inconsistent performance on margin as the bank focused on high growth.
- The other encouraging feature is the improvement in the CASA ratio to 39% as of March 2008 from 36% as of December 2007. Likely subdued deposit growth of 14% in 4QFY08 compared to 31% in 3QFY08 was likely a key contributor to this outcome.

**Non-interest income remains healthy aided by treasury profits**

- J&K Bank had a non-interest income (adjusted for investment amortization) of Rs866 mn (up 14% yoy).
- Treasury income increased by close to 3.6X to Rs350 mn in 4QFY08 and was the main contributor of this income.
- A key negative development in the current quarter was the decline in commission charges effected by J&K government in this quarter, which led to an overall decline in fee income by 57% yoy in 4QFY08.
- The company appears to be maintaining its growth momentum in fee income from the distribution of insurance products. Income from this activity increased to Rs81 mn in 4QFY08 compared to Rs48 mn in 4QFY07 and Rs66 mn in 3QFY08.

**Operating expenses decline and reasons appear unclear**

- J&K Bank had operational expenses of Rs1 bn in 4QFY08—a decline of 7% yoy.
- Employee expenses in the quarter were Rs436 mn, which contrasts with the run-rate of Rs600 mn per quarter reported in the first three quarters of FY2008 and Rs550 mn per quarter reported in the whole of FY2007. We remain unclear on the reasons for the behavior of this expense line.
- We note that J&K Bank has a transitional liability of Rs1.5 bn as of March 2007 for meeting the employee benefits under the revised AS-15 accounting norms. The company has decided to amortize the same over a five year period and has made the necessary provision in the current quarter. These provisions were recorded as an employee expense by the company.

**Asset quality remains healthy, while provision cover declines**

- J&K Bank had gross NPLs of Rs4.8 bn as of March 2008 – a marginal decline of 3% on a yoy basis and an increase of 4% marginally. The gross NPL ratio for the company was a healthy 2.5% compared to 2.9% as of March 2007.
- A less-than-healthy development at the company has been steady decline in the provision coverage ratio to 58% as of March 2008 from 73% as of June 2006. The company attributes this to good recoveries and reduction in the bad loans in its 'doubtful and loss category' loans. Net NPL ratio of the company was 1.1% as of March 2008.

## J&amp;K Bank quarterly performance, Rs mn

	4QFY07	1QFY08	2QFY08	3QFY08	4QFY08	% chg	4QFY08KS	Actual Vs KS
Interest income	5,210	5,751	5,967	6,183	6,442	23.6	6,635	(2.9)
Loans	3,754	4,402	4,600	4,810	4,963	32.2	5,012	(1.0)
Investments	1,368	1,266	1,325	1,364	1,458	6.6	1,600	(8.9)
Balance with RBI & banks	88	82	42	8	21	(76.3)	23	(10.1)
Interest expense	3,187	3,854	4,016	4,169	4,198	31.8	4,480	(6.3)
<b>Net interest income</b>	<b>2,024</b>	<b>1,896</b>	<b>1,951</b>	<b>2,013</b>	<b>2,244</b>	<b>10.9</b>	<b>2,155</b>	<b>4.1</b>
<b>Non-int.income</b>	<b>760</b>	<b>418</b>	<b>641</b>	<b>765</b>	<b>866</b>	<b>14.0</b>	<b>442</b>	<b>95.9</b>
Other income exld treasury	683	398	466	475	514	(24.7)	428	20.1
Treasury income	77	21	175	290	352	358.9	14	2,364.3
<b>Total income</b>	<b>2,784</b>	<b>2,314</b>	<b>2,592</b>	<b>2,778</b>	<b>3,110</b>	<b>11.7</b>	<b>2,597</b>	<b>19.7</b>
Operating expenses	1,094	943	1,034	1,039	1,021	(6.7)	1,280	(20.3)
Employee cost	599	610	599	613	436	(27.2)	694	(37.1)
Other cost	495	333	436	426	585	18.1	587	(0.3)
<b>Operating profit pre provisio</b>	<b>1,690</b>	<b>1,372</b>	<b>1,558</b>	<b>1,739</b>	<b>2,089</b>	<b>23.6</b>	<b>1,317</b>	<b>58.6</b>
Provisions and cont.	680	250	100	148	501	(26.4)	313	60.1
Investment Depreciation	145	-	-	-	192	33.1	-	-
Credit provisions	454	190	40	86	229	(49.4)	254	(9.8)
Standard asset provisions	334	90	40	80	36	(89.4)	-	-
PBT	1,010	1,122	1,458	1,592	1,589	57.3	1,004	58.2
Tax	557	289	380	500	990	77.8	487	103.5
<b>Net profit</b>	<b>453</b>	<b>832</b>	<b>1,078</b>	<b>1,092</b>	<b>598</b>	<b>32.1</b>	<b>517</b>	<b>15.6</b>
Tax rate (%)	55.2	25.8	26.1	31.4	62.3	-	48.5	-
<b>PBT-invt gains+ Prov</b>	<b>1,554</b>	<b>1,291</b>	<b>1,323</b>	<b>1,390</b>	<b>1,677</b>	<b>7.9</b>	<b>1,243</b>	<b>34.9</b>
<b>Key balance sheet items (Rs bn)</b>								
Total Deposits	252	247	260	265	286	13.5	-	-
Savings deposits	58	59	60	61	69	18.0	-	-
Current deposits	35	30	32	34	43	23.5	-	-
Term deposits	159	159	168	170	174	9.6	-	-
CASA ratio (%)	37.0	35.8	35.2	36.0	39.2	-	-	-
Advances	171	174	181	183	189	10.6	-	-
Investments	74	77	80	82	-	(100.0)	-	-
AFS	18	22	21	19	24	27.7	-	-
HTM	55	56	58	62	64	15.0	-	-
Assets	286	282	293	301	328	14.3	-	-
<b>Asset quality details</b>								
Gross NPLs (Rs mn)	5,018	4,872	4,778	4,686	4,852	(3.3)	-	-
Gross NPL ratio (%)	2.9	2.8	2.6	2.5	2.5	-	-	-
Net NPLs (Rs mn)	1,936	1,693	1,652	1,502	2,036	5.2	-	-
Net NPL ratio (%)	1.1	1.0	0.9	0.8	1.1	-	-	-
<b>Yield management measures (%)</b>								
Cost of Deposits (Annualised)	5.58	5.93	6.14	6.19	5.91	-	-	-
Yield on Advances (Annualised)	9.41	10.23	10.38	10.58	10.68	-	-	-
Yield on Investments (Annualised)	6.20	6.71	6.75	6.75	6.70	-	-	-
Net Interest Margins (Annualised)	3.36	2.90	2.97	2.98	3.18	-	-	-
<b>Capital adequacy details (%)</b>								
CAR	13.24	13.01	12.86	13.82	12.80	-	-	-
Tier I	12.60	12.37	12.19	13.12	12.14	-	-	-
Tier II	0.64	0.64	0.67	0.70	0.66	-	-	-
<b>Balance sheet snapshot (Rs mn)</b>								
Capital	485	485	485	485	485	-	-	-
Reserves and surplus	19,602	19,602	19,602	22,604	22,604	15.3	-	-
Deposits	251,943	247,437	259,539	265,270	285,933	13.5	-	-
Borrowings	6,202	6,902	4,131	4,187	7,518	21.2	-	-
Other liabilities and provisions	8,233	7,484	9,379	7,961	11,020	33.9	-	-
<b>Total</b>	<b>286,465</b>	<b>281,910</b>	<b>293,136</b>	<b>300,507</b>	<b>327,560</b>	<b>14.3</b>		
Cash and balance with RBI	18,548	15,377	21,785	17,128	32,200	73.6	-	-
Balance with banks etc	17,590	10,121	3,856	11,706	12,173	(30.8)	-	-
Investments	73,922	77,042	79,895	81,770	87,577	18.5	-	-
Advances	170,799	173,512	181,019	182,867	188,826	10.6	-	-
Fixed assets	1,834	1,844	1,897	1,950	1,920	4.7	-	-
Other assets	3,772	4,014	4,685	5,086	4,865	29.0	-	-
<b>Total</b>	<b>286,465</b>	<b>281,910</b>	<b>293,136</b>	<b>300,507</b>	<b>327,560</b>	<b>14.3</b>		

Source: Company.

**J&K Bank old and new estimates (Rs mn)**

March fiscal year-ends, 2008E-2010E

	Old estimates			New estimates			% change		
	2008E	2009E	2010E	2008E	2009E	2010E	2008E	2009E	2010E
Net Interest income	8,016	9,759	12,306	8,104	9,561	11,254	1.1	(2.0)	(8.5)
NIM (%)	2.56	2.60	2.83	2.71	2.75	2.80			
Loan (Rs bn)	209	249	290	189	228	270	(9.9)	(8.5)	(7.2)
Other income	2,266	1,958	2,315	2,690	1,939	2,309	18.7	(1.0)	(0.3)
Fee	1,078	1,207	1,352	851	979	1,126	(21.0)	(18.9)	(16.7)
Treasury	500	-	150	958	-	150			
Total income	10,282	11,717	14,621	10,795	11,500	13,563	5.0	(1.9)	(7.2)
Operating expense	4,296	4,982	5,633	4,036	4,708	5,459	(6.0)	(5.5)	(3.1)
Employee expense	2,515	2,933	3,271	2,258	2,631	3,065	(10.2)	(10.3)	(6.3)
Other expense	1,780	2,048	2,362	1,778	2,077	2,395	(0.1)	1.4	1.4
Provisions	810	1,568	2,851	999	1,464	2,662	23.2	(6.7)	(6.6)
NPLs	570	1,376	2,698	545	1,251	2,488	(4.4)	(9.1)	(7.8)
Invnt depreciation	-	-	-	192	-	-			
Invnt amortization	240	192	154	240	192	154			
PBT	5,176	5,167	6,136	5,760	5,329	5,441	11.3	3.1	(11.3)
Tax	1,656	1,653	1,964	2,160	1,705	1,741	30.4	3.1	(11.3)
<b>PAT</b>	<b>3,519</b>	<b>3,514</b>	<b>4,173</b>	<b>3,600</b>	<b>3,623</b>	<b>3,700</b>	<b>2.3</b>	<b>3.1</b>	<b>(11.3)</b>
PBT - treasury + provisions	5,246	6,543	8,684	5,540	6,579	7,779	5.6	0.6	(10.4)

Source: Kotak Institutional Equities estimates.

**Property****DLF.BO, Rs583**

Rating	BUY
Sector coverage view	Neutral
Target Price (Rs)	850
52W High -Low (Rs)	1225 - 490
Market Cap (Rs bn)	993.1

**Financials**

March y/e	2008	2009E	2010E
Sales (Rs bn)	142.5	180.0	224.0
Net Profit (Rs bn)	78.7	95.0	106.2
EPS (Rs)	46.2	55.7	62.3
EPS <i>gth</i>	263.6	20.7	11.8
P/E (x)	12.6	10.5	9.4
EV/EBITDA (x)	11.1	9.0	7.2
Div yield (%)	0.9	1.2	1.7

**Shareholding, March 2008**

	% of		Over/(under)
	Pattern	Portfolio	weight
Promoters	88.2	-	-
FIs	7.6	1.1	(1.8)
MFs	0.4	0.3	(2.6)
UTI	-	-	(2.9)
LIC	-	-	(2.9)

**DLF Limited: Recent sharp correction provides a good buying opportunity; reiterate BUY**

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- **Concerns on receivables will get diluted as customer payments flow in**
- **Current stock price implies a correction of more than 25% in selling prices**
- **Revenue mix for DLF to undergo substantial change over the next three years**
- **Our target price of Rs850 implies 40%+ upside; reiterate BUY**

We believe the recent correction in DLF stock price led by concerns over upward movement in non-DAL (DLF Assets Limited) receivables in 4QFY08 and correction in selling prices provides a good buying opportunity. We expect the receivable number of days to come down as DLF receives customer payments with progress in construction of various projects. The current stock price of Rs583/share is implying a sharp correction of 25% prices for real estate, which we believe is unlikely. We highlight that revenue mix for DLF to undergo substantial change over the next three years, which would reduce the risk profile of the business as it reduces the exposure to any one segment in the real estate space. DLF continues to be our top pick in the sector with (1) low D/E of 0.6X as of Mar '08, (2) solid execution with more than 60 mn sq. ft under execution, (3) higher NAV realization in the near term, (4) location superiority, and (5) reasonable valuations. We reiterate our BUY rating on the stock with a target price of Rs850 based on our Mar '09 based NAV of Rs675/share and terminal value of Rs175/share.

**Receivables rise largely because of accounting policy; will improve as customer payments flow in**

The concern largely has been the sharp upward trend in DLF receivables over the past four quarters (Exhibit 1). We highlight that out of receivables of Rs79 bn, only Rs19.4 bn is owed by DAL while rest of the receivables is on account of non-DAL residential and commercial complexes. The increase in non-DAL receivables is because of DLF's accounting policy. DLF books revenues on percentage completion based on total project cost (construction cost + land cost). In many projects, land cost constitutes significant proportion of total project cost and this leads to large revenue booking from these projects even at initial stages of completion. On the other hand, customer payments are usually linked to construction and hence accrue over time. This timing difference between revenue booking and customer payments leads to build-up of receivables. Exhibit 2 shows an example which explains this timing difference.

Hence, we are not overly worried about the increase in non-DAL receivables since we expect the receivable number of days to come down as DLF receives customer payments with progress in construction of various projects. We expect receivable situation to start improving from 2QFY09.

**Current stock price implying very high correction in selling prices**

Exhibit 3 shows that the current market price of Rs583/share is implying a correction of more than 25% in selling prices for all segments (residential, commercial and retail) in FY2009E, which we believe is quite large. We do not anticipate such large correction across all segments considering the demand-supply situation. A 25% correction in residential selling prices along with higher incomes, tax cuts and stable interest rates will lead to 35%+ increase in affordability triggering large demand. In commercial space, DLF already has pre-leased 16 mn sq. ft indicating healthy demand. In our model, we factor in a 10% correction in residential prices in FY2009E, stable prices in FY2010E and 5% growth thereafter. For retail/commercial, we assume stable prices in FY2009E and FY2010E and a 5% growth thereafter.

### Diversity in earnings to become more visible in the next three years

With the success of mid-income housing launches in Chennai, Kolkata and New Gurgaon, we expect residential segment to show solid numbers in FY2009E and FY2010E. We expect residential segment to grow from Rs37.6 bn in FY2008 to Rs95.4 bn in FY2010E, which would imply that it will contribute 41.8% to total revenues in FY2010E compared to 26.4% in FY2008 (see Exhibit 4). With 38 mn sq. of commercial space under execution, the commercial segment would continue to show good numbers. We estimate commercial revenues of Rs99.2 bn (both for lease and sale model) in FY2010E. DLF is also constructing 12 mn sq. ft of malls in prime shopping locations, which will become operational in FY2011 and will likely generate lease rentals of Rs28.4 bn. The hotels business will also likely contribute to revenues in FY2011E.

### Top pick in the sector: Healthy balance sheet; execution continues to be solid

We prefer DLF because of its low balance sheet leverage, which would help in the current scenario where financial markets remain volatile and residential markets remain under strain. Exhibit 5 shows that DLF has a D/E of 0.6X as of Mar '08 which is one of the lowest in the sector. We highlight that execution of DLF remains solid with area under execution increasing to 61.5 mn sq. ft in 4QFY08, 25% increase over 1QFY08 (Exhibit 6).

### Retain BUY with a target price of Rs850/share

Our March '09-based NAV for DLF is Rs675/share. We have assigned a terminal value of Rs175/share since DLF has shown a track record of investing in new projects at high IRRs. Our terminal value is based on 1X FY2011E adj. P/B discounted back to Mar '09. For calculating terminal value we now adjust FY2011E net worth with outstanding receivables since we have observed that actual cashflows are lagging behind revenues. We highlight that DLF is already investing into new large projects like hotels, SEZs and townships that will start contributing to revenues in a few years.

**Should there be premium to NAV/terminal value?** Yes, real estate companies should get terminal value as is the case with most sectors but only when a company has shown a track record of execution and continuous land bank replenishment. Valuing a company only based on its NAV will not give due credit to a company's franchise value or its ability to create value for its shareholders as a going concern. We believe the terminal value of a company should be linked to its investment ability as real estate companies need to buy more land in order to earn profits in future years.

### DLF has 165 days of receivables at end 4QFY08

	FY2008			
	Q1	Q2	Q3	Q4
Revenues (Rs mn)	30,740	32,500	35,980	43,060
Receivables	37,478	38,936	64,790	79,075
<b>Receivables (No of days)</b>	<b>110</b>	<b>108</b>	<b>162</b>	<b>165</b>

Source: Company, Kotak Institutional Equities.

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**Revenue booking occurs faster on project cost accounting bas**

<b>Selling price</b>	(Rs/sq. ft)	15,000
<b>Land Cost</b>	(Rs/sq. ft)	5,000
<b>Construction cost</b>	(Rs/sq. ft)	2,500
<b>Customer payments</b>	Linked to construction schedule	

		<b>Project cost basis</b>	<b>Construction cost basis</b>
<b>Construction incurred</b>	(%)	10	10
<b>Customer payments (a)</b>	(Rs/sq. ft)	1,500	1,500
<b>Cost incurred (I)</b>	(Rs/sq. ft)	5,250	250
<b>Relevant total cost (II)</b>	(Rs/sq. ft)	7,500	2,500
<b>Percentage completion ((I)/(II))</b>	(%)	70	10
<b>Revenues booked (b)</b>	(Rs/sq. ft)	10,500	1,500
<b>Receivables ((b)-(a))</b>	(Rs/sq. ft)	9,000	-

Source: Kotak Institutional Equities

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**Current stock price implying correction of more than 25% in selling prices**

Sensitivity of fair value (Rs/share) to reduction in selling prices (%)

	<b>Fair value(Rs/share) based on</b>	
	<b>NAV</b>	<b>NAV + Terminal value</b>
<b>Reduction in FY2009E selling prices (%)</b>		
5	661	834
10	619	782
15	576	729
20	534	677
25	491	625
30	448	573

Note:

(a) WACC =13%.

(b) The reduction in selling prices refers to all segments-residential, commercial and retail.

Source: Kotak Institutional Equities estimates.

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**Revenue model of DLF, March fiscal year-ends (Rs mn)**

	2007	2008E	2009E	2010E	2011E
<b>Housing</b>					
Housing volumes (mn sq. ft)	1.9	8.0	12.9	21.3	30.8
Revenues	9,832	37,631	66,742	95,417	120,806
Rate/sq. ft	5,166	4,686	5,190	4,477	3,917
<b>Commercial</b>					
Commercial volumes (mn sq. ft)	4.3	8.0	10.0	13.6	14.9
Revenues	18,411	55,817	72,145	90,008	103,975
Rate/sq. ft	4,286	6,965	7,223	6,636	6,983
<b>Retail (Sold)</b>					
Retail volumes (mn sq. ft)	0.7	2.7	1.6	1.6	1.4
Revenues	7,216	40,456	22,018	17,659	10,287
Rate/sq. ft	10,067	15,015	13,397	11,300	7,537
<b>Retail (leased)</b>					
Cumulative volumes (mn sq. ft)			1.3	1.3	13.4
Revenues			4,173	4,173	28,391
Rate/sq. ft/month			272	272	177
<b>Commercial (leased)</b>					
Cumulative volumes (mn sq. ft)	3.0	3.0	7.7	12.1	19.7
Revenues	1,546	3,010	7,248	9,161	13,955
Rate/sq. ft/month	50	60	63	77	73
<b>Revenue from real estate</b>	<b>37,004</b>	<b>136,914</b>	<b>172,325</b>	<b>216,418</b>	<b>277,414</b>
Others	2,200	5,611	7,635	7,569	11,792
<b>Revenues</b>	<b>39,204</b>	<b>142,525</b>	<b>179,960</b>	<b>223,987</b>	<b>289,206</b>
% growth	240	264	26	24	29

**Revenue mix (%)**

Housing	25.1	26.4	37.1	42.6	41.8
Commercial	47.0	39.2	40.1	40.2	36.0
Retail	18.4	28.4	12.2	7.9	3.6
Leased properties	3.9	2.1	6.3	6.0	14.6
Others	5.6	3.9	4.2	3.4	4.1
<b>Total</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>

Source: Company, Kotak Institutional Equities estimates.

**Healthy balance sheet to be a key differentiator**

D/E based on debt (in Rs bn) and equity (in Rs bn) as of Mar 2007 and Dec 2007

	As of Mar 31, 2008					As of Dec 31, 2007					As of Mar 31, 2007				
	Cash (bn)	Debt (bn)	Net debt (bn)	Equity (bn)	D/E (X)	Cash (bn)	Debt (bn)	Net debt (bn)	Equity (bn)	D/E (X)	Cash (bn)	Debt (bn)	Net debt (bn)	Equity (bn)	D/E (X)
DLF	19.4	122.6	103.2	205.8	0.6	7.8	92.4	84.6	176.8	0.5	4.2	99.3	95.2	35.5	2.8
Unitech	—	—	—	—	—	25.0	70.0	45.0	32.9	2.1	10.2	39.8	29.6	19.9	2.0
HDIL	3.5	31.1	27.6	36.4	0.9	8.5	16.9	8.4	30.0	0.6	0.0	3.8	3.7	7.3	0.5
Sobha	0.8	17.6	16.8	9.9	1.8	2.5	15.0	12.5	9.7	1.5	0.2	5.8	5.6	8.2	0.7
Purvankara	0.3	6.5	6.2	12.1	0.5	1.3	4.4	3.1	11.9	0.4	0.4	6.8	6.4	2.2	3.0
Parsvnath	—	—	—	—	—	5.3	18.1	12.9	18.1	1.0	5.5	11.7	6.2	14.9	0.8

Source: Company, Kotak Institutional Equities.

**Commercial segment continues to be the major driver, residential segment ramping up**  
Segment-wise area under development (mn sq. ft)

	Area under development (mn sq. ft)			
	Q1	Q2	Q3	Q4
Residential	6.7	6.7	7.0	12.1
Commercial	29.5	34.4	39.8	38.2
Retail	13.0	13.4	11.6	11.2
<b>Total</b>	<b>49.2</b>	<b>54.6</b>	<b>59.0</b>	<b>61.5</b>

Source: Company, Kotak Institutional Equities.

**Our estimate for DLF's NAV is Rs675/ share**

NAV sensitivity to growth rate in selling prices (Rs bn)

Valuation Methodology	March '09 based NAV Growth rate in selling prices			
	0%	3%	5%	10%
<b>Valuation of land reserves</b>	<b>880</b>	<b>973</b>	<b>1,061</b>	<b>1,234</b>
Residential	267	306	336	421
Retail	272	304	327	392
Commercial	341	363	378	421
Add: 22 Hotel sites	2X land acquisition cost	50	50	50
Add: Construction JV	15X FY2009E P/E	30	30	30
Add: Other properties (plots in Gurgaon - 7.2 mn sq. ft, hotel site in Gurgaon)	Current market value	22	22	22
Add: Present value of project management fees		8	8	8
Add: Investments as on March 31, 2008		20	20	20
Add: Bidadi township		40	40	40
Less: Net debt as on March 31, 2008		(104)	(104)	(104)
Less: Land cost to be paid as on March 31, 2008		(30)	(30)	(30)
<b>NAV (Rs bn)</b>	<b>981</b>	<b>1,074</b>	<b>1,162</b>	<b>1,335</b>
<b>NAV/share (Rs)</b>	<b>570</b>	<b>623</b>	<b>675</b>	<b>775</b>
<b>Terminal value (Rs bn)</b>	1X FY2011E adj. P/B discounted to March 2009	<b>301</b>	<b>301</b>	<b>301</b>
Total no. of shares including ESOPs of 17 mn shares (mn)				1,722
<b>Valuation/share (Rs)</b>				<b>850</b>

Source: Kotak Institutional Equities estimates.

**Technology****TEML.BO, Rs821**

Rating	ADD
Sector coverage view	Neutral
Target Price (Rs)	900
52W High -Low (Rs)	1563 - 575
Market Cap (Rs bn)	102.3

**Financials**

March y/e	2008	2009E	2010E
Sales (Rs bn)	37.7	50.2	63.2
Net Profit (Rs bn)	7.8	9.3	11.1
EPS (Rs)	59.1	71.0	84.4
EPS <i>gth</i>	25.7	20.3	18.7
P/E (x)	13.9	12	9.7
EV/EBITDA (x)	12.4	8.7	6.7
Div yield (%)	0.5	0.6	0.8

**Tech Mahindra: Notes from management meetings—revenue visibility remains the key focus area. Maintain ADD**

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- **BT revenues—multi-year large deal signings should address market share loss concerns**
- **Large deals—more than just revenue assurance; provides opportunities for margin management**
- **Margin concerns on BTGS (and other large deals) overplayed; we do not like the aggressive accounting treatment, though**
- **Maintain ADD with a target price of Rs900/share**

We highlight the key takeaways from the series of investor meetings we organized with the Tech Mahindra (TM) management recently—(1) the company remains focused on increasing revenue visibility; this reflects in the recent multi-year large deals signed, (2) the management is confident that the US\$1-bn BTGS deal will generate corporate-average margins (after accounting for the upfront payment) over the course of the deal, (3) the non-BT portfolio continues to grow strong; we note that the company recently signed a US\$170-220 mn seven-year deal with a large US-based TSP recently, and (4) increasing revenue productivity (or de-linking revenue and headcount growth, in other words) remains a top priority. We believe TM provides reasonable revenue visibility, aided by strong spending tailwinds in the TSP vertical and TM's strong positioning within key accounts. However, profitability will continue to be volatile as TM bears transition costs on large deals. We maintain our ADD rating on the stock with a target price of Rs900/share. The stock is trading at 11.6X FY2009E and 9.7X FY2010E earnings (11.2X FY2010E earnings adjusted for amortization costs). Key upside risk is better-than-expected margin performance.

**BT revenues—multi-year large deal signings should address market share loss concerns.** TM management emphasized that the recently announced five-year, US\$350 mn (US\$100 mn incremental) apps deal with BT (core), in addition to increased visibility on the earlier US\$1 bn deal signed with BTGS should allay some of the investor concerns about a potential loss in market share within the BT account. We have highlighted in the past that TM is among the top two vendors in 14 of BT's 15 platforms. We believe TM is on a strong footing within the BT account and expect robust growth in BT revenues for TM over the next two years. We forecast a 28% and 18% growth in the BT revenues for TM in FY2009E and FY2010E, respectively.

**Large deals—more than just revenue assurance; provides opportunities for margin management.** TM management highlighted the strategic long-term intent behind the two large deals signed with BT

- **US\$1-bn BTGS deal.** The five-year with BT Global Services gave TM a foothold in the Enterprise business of BT. BTGS has been (and is expected to continue to be) the revenue growth driver for BT over the coming years. While the discovery and learning phase on the deal (this was the first large Enterprise business contract for TM) has taken longer than initially expected (four quarters versus two), TM management emphasized that the deal will enhance TM's credibility in the Enterprise space and position the company better to bid for deals in this space from other TSPs.

- **US\$350 mn deal with BT core.** TM management indicated that the recent US\$350 mn (US\$100 mn incremental) five-year deal with BT (core) provides three key benefits to TM—(1) converts its existing US\$50 mn per annum business (from multiple contracts) to an annuity revenue stream for at least five years; TM would have had to renegotiate each of these multiple contracts in the absence of such a deal, (2) the incremental US\$20 mn per annum business implies marginal market share gain, and (3) the long-term nature of the contract allows TM to invest in automation and other productivity tools to ensure healthy operating margins; short-term deals do not allow this flexibility.

**Margin concerns on BTGS (and other large deals) overplayed; we do not like the aggressive accounting treatment, though.** TM management reiterated that the profitability of the US\$1-bn BTGS deal (after accounting for the upfront payment of US\$118 mn) will be close to the corporate-average profitability (FY2008 EBIT margin was 20%) over the course of the deal. We highlight some of the likely factors driving management's confidence: (1) TM would be able to capture productivity investments through the course of the contract (and not pass the same on to BT in the form of volume discounts or lower pricing, as is the case with typical contracts), and (2) the long-term nature of the deal provides substantial headroom for investing in tools/automation, to drive higher productivity and/or lower cost of service delivery.

Our concern on the upfront-payment deal structure that TM has entered into center around the aggressive accounting treatment of these payments. TM had taken an exceptional charge of US\$118 mn pertaining to the US\$1-bn BTGS deal in 4QFY07. The company also took an exceptional charge of US\$110 mn in 4QFY08 for a 90-day exclusive negotiation right (with a consortium partner) for another large deal with BT. We find the accounting treatment of these payments extremely aggressive and illogical; the management indicates that accounting treatment was consistent with the auditor's recommendations. We believe this treatment does not yield itself favorably to revenue-cost matching principle (inflates profitability in the later years of the contract by not amortizing the upfront payment costs over the course of the contract).

**Non-BT relationships—strong on TSP's, weakness in TEMs.** TM continues to drive strong growth from its non-BT relationships; non-BT revenues have grown 3.7X over the past two years (a fact that often goes unnoticed with the 3.2X growth in BT revenues over the same timeframe). We do highlight, however, that TM has seen some weakness in its TEM clients in the recent quarters (in line with the other players in the industry); the qoq decline in non-BT revenues in 4QFY08 was partially on account of weakness in some TEM clients. Among non-BT TSPs, AT&T (11.5% of revenues, US\$100mn+ relationship) continues to grow strong. TM has won several marquee non-BT clients over the past few quarters, the most notable wins being Telecom Newzealand, and top TSPs in Canada. TM also recently signed a US\$170-220 mn seven-year deal with a large US-based TSP. We believe the marquee client portfolio, in addition to the strong capex tailwinds in the TSP vertical provides TM an excellent opportunity to grow its non-BT revenues over the next few years. TM needs to scale up its efforts in this area as the BT and AT&T relationships could peak out in the next two to three years. We forecast a 45% and 40% growth in non-BT revenues for TM in FY2009E and FY2010E, respectively.

**Tech Mahindra—consolidated Indian GAAP profit & loss statement. March fiscal year-ends (Rs mn)**

	2006	2007	2008	2009E	2010E
<b>Revenues</b>	<b>12,427</b>	<b>29,290</b>	<b>37,661</b>	<b>50,208</b>	<b>63,193</b>
Direct cost	(7,397)	(17,536)	(23,854)	(31,913)	(40,858)
<b>Gross profit</b>	<b>5,030</b>	<b>11,754</b>	<b>13,807</b>	<b>18,296</b>	<b>22,334</b>
SG&A expenses	(2,351)	(4,387)	(5,549)	(7,271)	(9,093)
<b>EBITDA</b>	<b>2,679</b>	<b>7,368</b>	<b>8,258</b>	<b>11,025</b>	<b>13,241</b>
Depreciation	(397)	(515)	(796)	(1,017)	(1,239)
<b>EBIT</b>	<b>2,282</b>	<b>6,852</b>	<b>7,462</b>	<b>10,007</b>	<b>12,001</b>
Other income	340	77	1,044	409	704
Interest		(61)	(62)	-	-
<b>Profit before tax</b>	<b>2,622</b>	<b>6,868</b>	<b>8,444</b>	<b>10,416</b>	<b>12,706</b>
Tax	(268)	(740)	(748)	(1,109)	(1,655)
<b>Net profit</b>	<b>2,354</b>	<b>6,128</b>	<b>7,696</b>	<b>9,307</b>	<b>11,050</b>
Minority interest	(0)	(1)			
<b>Net income</b>	<b>2,354</b>	<b>6,127</b>	<b>7,696</b>	<b>9,307</b>	<b>11,050</b>
Extraordinaries	-	(4,910)	(4,401)	-	-
<b>Net profit- reported</b>	<b>2,354</b>	<b>1,218</b>	<b>3,295</b>	<b>9,307</b>	<b>11,050</b>
<b>Fully Diluted EPS (Rs/Share)</b>		<b>47.0</b>	<b>59.0</b>	<b>71.0</b>	<b>84.4</b>
<b>Margins (%)</b>					
Gross profit margin	40.5	40.1	36.7	36.4	35.3
EBITDA margin	21.6	25.2	21.9	22.0	21.0
EBIT margin	18.4	23.4	19.8	19.9	19.0
NPM	18.9	20.9	20.4	18.5	17.5
<b>Growth rates (%)</b>					
Revenues	31.4	135.7	28.6	33.3	25.9
Gross profit	44.4	133.7	17.5	32.5	22.1
EBITDA	98.4	175.0	12.1	33.5	20.1
EBIT	121.8	200.3	8.9	34.1	19.9
Net profit	130.1	160.3	25.6	20.9	18.7

Source: Kotak Institutional Equities estimates.

**Pipes****PSLH.BO, Rs353**

Rating	BUY
Sector coverage view	Attractive
Target Price (Rs)	500
52W High -Low (Rs)	610 - 233
Market Cap (Rs bn)	14.6

**Financials**

March y/e	2008	2009E	2010E
Sales (Rs bn)	21.8	30.7	38.3
Net Profit (Rs bn)	1.1	1.7	2.3
EPS (Rs)	28.4	40.5	55.8
EPS <i>gth</i>	40.1	42.9	37.7
P/E (x)	12.4	8.7	6.3
EV/EBITDA (x)	7.8	5.7	4.1
Div yield (%)	1.6	1.8	2.0

**Shareholding, March 2008**

	% of Pattern Portfolio	Over/(under) weight
Promoters	48.4	-
FIs	17.4	0.0
MFs	14.4	0.1
UTI	-	-
LIC	-	-

**PSL: US subsidiary wins \$418 mn order, boosts order book to Rs42 bn; reiterate BUY**

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- **US subsidiary adds its first order of US\$418 mn (62% of earlier order book) for gas pipeline**
- **Order size of 220,000 tons—higher than our estimated volumes of 161,000 tons over FY2009-10E from the USA plant**
- **Large order addition increases revenue visibility; current order book at Rs42 bn against estimated revenues of Rs3.4 bn for FY2009E**
- **Reiterate BUY with target price of Rs500; will revise estimates post 4QFY08 results**

PSL has received a US\$418 mn order from Florida Gas Transmission Company for the supply of 543 miles of coated HSAW pipe increasing the order book by 62% to Rs42 bn. Large increase in order book provides strong support to our revenue estimates for FY2009E and FY2010E as current order book provides visibility for next 1.3 years. We highlight that the volumes and realizations from the order added in USA are much higher than our estimated volumes and realizations, which could result in higher-than-expected revenues and margins in FY2009 and FY2010. However, pending award of API approval for PSL's US plant and commencement of production for the latest order, we do not revise our estimates yet. Furthermore, if the recent issued 10% export duty on linepipes stays, PSL will be the least impacted as its exports from India represent only 2% of the current order book. We maintain our estimates, BUY recommendation and target price of Rs500.

**US subsidiary bags large order of US\$418 mn; first major order from North America**

PSL through its US subsidiary—PSL North America LLC has won a large order for US\$418 mn from Florida Gas Transmission Company in USA to supply 543 miles (870 km) of coated HSAW pipes. As per the project documents filed with Federal Energy Regulatory Commission (FERC), this is largely for a 36" diameter coated gas pipeline. We estimate the total order to be approximately for 220,000 tons implying a realization of about US\$1,900 / ton (versus our FY2009E average realization estimate of US\$1,400/ton). We expect this order to contribute incrementally better margins than PSL's overall margins reported over the past few quarters. PSL expects to service this order from the upcoming 300,000 tons plant in USA which is likely to commence operation by Aug '08. Management expects deliveries to begin in Jan 2009 and complete by end-CY2009. The order size of around 220,000 tons is higher than our estimated volumes of 161,000 tons over FY2009-10E. However, we do not revise our assumptions—volumes, revenues and margins—yet, pending commercialization of the plant and API approval.

**US market—strong realizations, but upcoming capacities may increase margin pressures**

We do not expect significant margin improvements for PSL from the USA plant as (1) it will be in the initial scale up period involving high costs and (2) upcoming competition may keep margin expansion under pressure despite of high demand. Demand and realization in US for linepipes continues to be strong due to supply shortages. However, we believe with 1.8 mn tons of HSAW capacity scheduled to come up over the next 12-18 months, increasing competition and supply could put pressure on realizations and margins. PSL's USA facility is expected to be the first to commence operations hence it may enjoy higher realizations during the initial period; however, as new capacities roll out, we expect linepipe conversion margins to stabilize or even fall marginally.

**Large order book of Rs42 bn supports strong revenue growth estimates**

PSL's current order book of Rs42 bn provides strong support to our revenue estimates of Rs30.6 bn and Rs38.3 bn for FY2009E and FY2010E, respectively. The US order will largely be completed in FY2010E hence providing greater visibility to our FY2010E estimates. We highlight PSL is the least impacted from the recently imposed 10% export duty on linepipes as only 2% of its current order book (see Exhibit 2) represents export of pipes from India. However, we currently do not model any export duty charges in our estimates, awaiting greater clarity on the regulation.

**India operations—awaiting large order announcements by GAIL**

In the domestic market, bids for GAIL's 300,000 tons order are expected to be opened this month. Approx 80,000 tons of the same is for >25 mm thickness which will be serviced by the LSAW players. Of the balance, PSL may win a majority portion based on its available large capacities. We believe this could provide further upside to our revenue estimates for FY2009E and support FY2010E growth assumptions. Further, tender for the 730 km Dabhol-Bangalore pipeline is expected to be opened in July '08, where again PSL may be one of the leading vendors considering its large unutilized capacities versus peers with limited available capacities.

**Strong expected order flow could warrant further capacity expansions**

We believe PSL may consider expanding capacities to meet the expected order flow. Management is considering expanding the UAE capacity to 300,000 tons from current 75,000 tons. It may also consider expanding capacities at one of its coastal plants in case domestic order flows pick up.

**Valuations—reiterate BUY with DCF-based target price of Rs500**

We find current valuations compelling—9.2X and 6.5X 2009E EPS and EBITDA, respectively. Strong order book provides visibility to near-term earnings and incremental orders provide further upside risk. We reiterate BUY rating and 12 month DCF-based target price of Rs500 (41% upside to current price). We maintain our estimates currently and will revise our volume and margin assumptions based on recent orders post the 4QFY08 results.

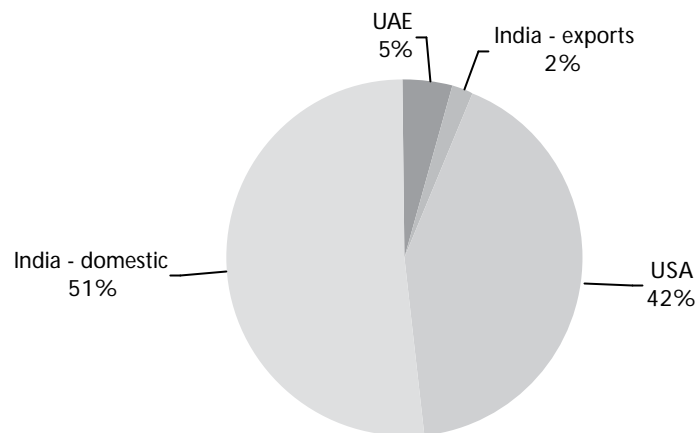
**Exhibit 1: Forecasts and valuation (consolidated)**

March year-end	Sales (Rs mn)	EBITDA (Rs mn)	Adj. PAT (Rs mn)	EPS (Rs)	RoAE (%)	P/E (X)	EV/EBITDA (X)
2006	14,503	1,550	519	14.1	22.6	25.2	12.1
2007	14,433	1,642	653	15.8	20.7	22.5	12.3
2008E	21,791	2,279	1,073	24.6	21.6	14.4	9.4
2009E	30,651	3,405	1,680	38.6	23.6	9.2	6.5
2010E	38,267	4,278	2,314	53.1	26.2	6.7	4.7

Source: Company data, Kotak Institutional Equities estimates.

**Exhibit 2: Order book break up for PSL**

Break up of PSL's current order book of Rs42 bn (%)



Source: Company, Kotak Institutional Equities.

**Exhibit 3: Operating assumption for PSL**

	2008E	2009E	2010E
<b>Sales ('000 tons)</b>			
India	341	440	528
UAE	11	32	38
USA	-	56	105
<b>Realisation (US\$/ton)</b>			
India	1,291	1,316	1,336
UAE	900	1,356	1,376
USA		1,400	1,421
<b>Raw material cost (US\$/ton)</b>			
HR coil	784	800	808
<b>EBITDA</b>			
EBITDA (Rs mn)	2,279	3,405	4,278
EBITDA / ton (\$)	152	159	158

Source: Kotak Institutional Equities estimates.



**Exhibit 4: Profit model, balance sheet, cash model for PSL Ltd 2005-2010E, March fiscal year-ends (Rs mn)**

	2005	2006	2007	2008E	2009E	2010E
<b>Profit model</b>						
Net revenues	14,092	14,503	14,433	21,791	30,651	38,267
<b>EBITDA</b>	<b>1,173</b>	<b>1,550</b>	<b>1,642</b>	<b>2,279</b>	<b>3,405</b>	<b>4,278</b>
Other income	170	193	274	364	341	397
Interest (expense)/income	(648)	(690)	(563)	(581)	(613)	(566)
Depreciation	(240)	(344)	(445)	(532)	(710)	(831)
<b>Pretax profits</b>	<b>454</b>	<b>708</b>	<b>908</b>	<b>1,530</b>	<b>2,424</b>	<b>3,279</b>
Tax	(102)	(192)	(280)	(396)	(664)	(762)
Deferred taxation	(20)	3	25	(61)	(63)	(46)
Minority Intt	—	—	—	—	(17)	(156)
<b>Adjusted consolidated net income</b>	<b>333</b>	<b>519</b>	<b>653</b>	<b>1,073</b>	<b>1,680</b>	<b>2,314</b>
<b>Diluted Earnings per share (Rs)</b>	<b>11.5</b>	<b>14.1</b>	<b>15.8</b>	<b>24.6</b>	<b>38.6</b>	<b>53.1</b>
<b>Balance sheet</b>						
Total equity	1,825	2,777	3,519	6,404	7,818	9,817
Deferred taxation liability	35	32	7	68	131	177
Total borrowings	6,490	6,810	6,698	6,961	7,654	5,558
Minority Interest	—	—	—	—	17	173
Current liabilities	4,817	5,898	5,791	7,656	9,980	12,222
<b>Total liabilities and equity</b>	<b>13,168</b>	<b>15,518</b>	<b>16,015</b>	<b>21,090</b>	<b>25,600</b>	<b>27,946</b>
Cash	1,796	1,199	1,263	1,000	1,000	1,000
Other current assets	8,477	10,654	9,596	13,153	17,588	20,609
Total fixed assets	2,793	3,564	5,131	6,912	6,987	6,313
Miscl. Exps. not w/o	0	0	0	—	—	—
Investments	102	102	25	25	25	25
<b>Total assets</b>	<b>13,168</b>	<b>15,518</b>	<b>16,015</b>	<b>21,090</b>	<b>25,600</b>	<b>27,946</b>
<b>Free cash flow</b>						
Operating cash flow, excl working capital	342	900	1,042	1,303	2,128	2,950
Working capital changes	(2,179)	(1,267)	695	(1,495)	(2,111)	(779)
Capital expenditure	(1,180)	(1,115)	(2,012)	(2,313)	(784)	(157)
Investments	(56)	—	77	—	—	—
Other income	12	41	142	364	341	397
<b>Free cash flow</b>	<b>(3,060)</b>	<b>(1,441)</b>	<b>(57)</b>	<b>(2,142)</b>	<b>(425)</b>	<b>2,411</b>
<b>Ratios (%)</b>						
Debt/equity		3.5	2.4	1.9	1.1	1.0
Net debt/equity		2.5	2.0	1.5	0.9	0.8
RoAE		18.3	22.6	20.7	21.6	23.6
<b>RoACE</b>		<b>13.2</b>	<b>11.4</b>	<b>10.7</b>	<b>12.5</b>	<b>14.5</b>

Source: Company, Kotak Institutional Equities estimates.

## Banking

Sector coverage view

Attractive

Company	Rating	Price, Rs	
		3-Jun	Target
SBI	ADD	1,388	1,800
HDFC	REDUCE	2,457	2,700
HDFC Bank	BUY	1,266	1,500
ICICI Bank	ADD	761	933
Corp Bk	ADD	336	375
BoB	ADD	248	335
PNB	BUY	472	650
OBC	ADD	175	210
Canara Bk	SELL	205	200
LIC Housing	REDUCE	334	350
Axis Bank	REDUCE	757	850
IOB	REDUCE	115	145
Shriram Transf	REDUCE	336	355
SREI	BUY	140	240
MMFSL	REDUCE	266	290
Andhra	REDUCE	75	81
IDFC	REDUCE	139	170
PFC	REDUCE	134	165
Centurion Bank	REDUCE	43	45
Federal Bank	BUY	211	310
J&K Bank	ADD	649	750
India Infoline	ADD	719	1,225
Indian Bank	ADD	116	150
Union Bank	BUY	129	210
Central Bank o	SELL	78	85

## RBI may tighten capital adequacy requirements and exposure norms prompted by rising risk on off-balance-sheet items

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- **RBI issues draft guidelines for off-balance-sheet exposure of banks given volatility in financial markets**
- **Credit exposure calculations for off-balance-sheet items for banks for exposure norms pertaining to individual companies and CAR to be similar**
- **Norms for calculating exposure have been tightened across product categories**
- **Key implications: (1) Some banks would have to scale down their exposure to individual corporates and (2) risk weights for most banks would increase, adversely impacting their CARs**

RBI has issued draft guidelines for the off-balance-sheet exposure of banks given the increased volatility in financial markets. Media reports indicate that banks like ICICI Bank, HDFC Bank, Axis Bank and SBI have been active participants in the derivative markets and have considerable exposure to this segment. The proposal envisages similar credit exposure calculations for off-balance-sheet items for banks for exposure norms pertaining to individual companies and to CAR. As a result, we believe some banks would have to scale down their exposure to individual corporates while risk weights for most banks would increase, thereby adversely impacting their capital adequacy ratios. We are unable to quantify the impact on the financials of banks given the lack of sufficient data on the exposure of individual banks to the various derivative products.

**The key changes proposed by RBI with regard to off-balance-sheet exposure of banks** are (1) the credit exposure calculations for off-balance-sheet items of banks for exposure norms to individual corporates and capital adequacy purposes are to be unified (earlier norms had disparate calculations for these two purposes); (2) the norms for calculating exposure have been tightened across product categories (exchange and interest rate products); (3) banks are to maintain standard asset provisions on their off-balance-sheet exposure, which could impact their profits. Banks have four quarters in which to prepare to adhere to these regulations. Meanwhile, banks are likely to approach RBI with suggestions on draft guidelines.

**Key implications of these guidelines**, in our view, are (1) some banks would have to scale down their exposure to individual corporates and (2) risk weights for most banks would increase, thereby adversely impacting their capital adequacy ratios. We are unable to quantify the impact on the financials of banks given the lack of sufficient data on the exposure of individual banks to the various derivative products.

**RBI has modified the exposure norms of banks to oil companies and reduced the mark-up required for valuing these non-SLR securities**—this move has been prompted by the continued rise in crude oil prices and the resulting increase in off-balance-sheet borrowings of the government. Bank exposure to individual oil companies has been enhanced to 25% of net worth, previously limited to 15%. Similarly, non-SLR securities are to be valued at a mark-up of 25 bps above the corresponding yield on Government of India securities, previously these were valued at 50 bps above the corresponding yield on Government of India securities.

**Automobiles**

Sector coverage view

Attractive

Company	Rating	Price, Rs	
		3-Jun	Target
Hero Honda	REDUCE	798	710
Tata Motors	SELL	570	525
Maruti Suzuki	BUY	782	1,000
Mah & Mah	ADD	594	720

**Freight rates rise in Apr '08, DAFI up 9.1% mom indicating a revival in CV volumes**

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- **DAFI up 9.1% mom—up 15.4% since its low in September '07**
- **Fuel price not to impact too much as freight operators would be able to pass on the hike in costs**
- **We continue to be positive on the CV cycle**

**DAFI up 9.1% mom—up 15.4% since its low in September '07**

Freight rates were up in Apr '08 resulting in our freight index rising 2.1% mom and 3.6% yoy. Our Diesel-Adjusted-Freight-Index (DAFI) rose by a sharp 9.1% mom and 5.4% yoy—the 9.1% mom growth in DAFI has been the highest increase in DAFI since Mar '07. On a cumulative basis, DAFI has risen 15.4% since its low in Sep '07. The DAFI has fallen 6.1% mom in Mar '08 on account of the hike in diesel prices by Rs1 in mid-Feb post which it has again moved up. Meanwhile, CV volumes have grown 7.6% yoy in Apr '08—M&HCVs have grown at 5.3% while the LCV segment has grown at 10.7% in Apr '08. We believe this is a positive trend indicating a revival in CV volumes in FY2009.

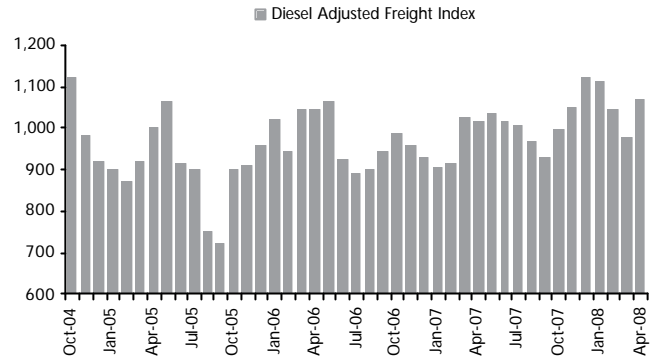
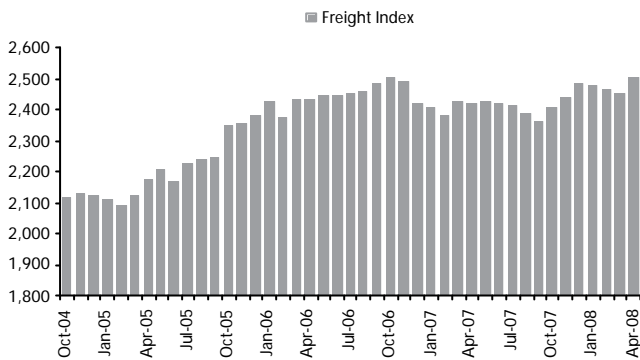
**Fuel price not to impact too much as freight operators would be able to pass on the hike in costs**

We believe any hike in the price of diesel would not impact the freight operators' profitability and they would be able to pass on the increase in operating costs on account of a rise in diesel price. Historical evidence suggests that a rise in diesel prices have always been passed on and rise in diesel price has not impacted freight operators' profitability. We believe given the demand for movement of freight using roads, the freight operator will be able to increase freight rates to match the increased fuel price. Moreover, our analysis suggests that freight rates would need to be increased 4.3% if the diesel price were to increase by Rs2/litre. We believe freight operators would be able to raise freight rates to the extent of 4-6% and hence absorb diesel price rise up to Rs2-3/litre. The second exhibit shows the required increase in freight rate to match the hike in diesel prices.

**We continue to be positive on the CV cycle**

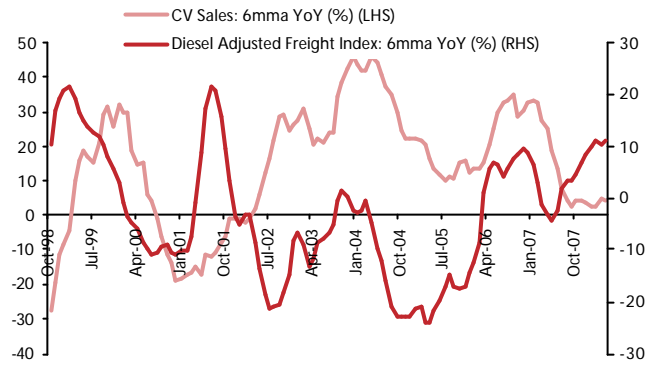
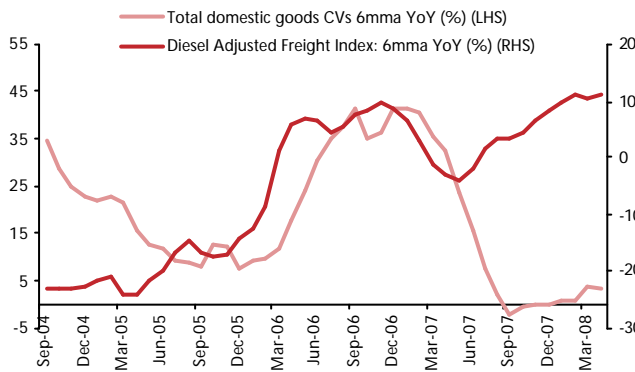
We believe freight rates would continue to be robust and any increase in fuel price will not likely dampen the demand for CVs as demand for road-freight is likely to remain strong. We continue to remain positive on the CV cycle. Our lead indicators have been suggesting a revival of CV volumes and we believe that demand for CVs should be strong—CV volumes have been growing since Feb '08. Besides, we do not see any signs of over-supply of CVs in the system. We expect the trend to continue. We believe the CV cycle should be positive in FY2009 and the industry should witness a robust growth in M&HCVs as well as LCVs.

**Freight index has gained 2.1% mom in Apr '08 while the DAFI was up 9.1% mom indicating robust freight operator profitability**



Source: Kotak Institutional Equities.

**Our lead indicators suggest revival of CV growth—we continue to be positive on CV cycle**



Source: SIAM, Kotak Institutional Equities.

**Freight rates need to increase 4.3% to maintain freight operator's profitability in the event of a Rs2 hike in diesel price**

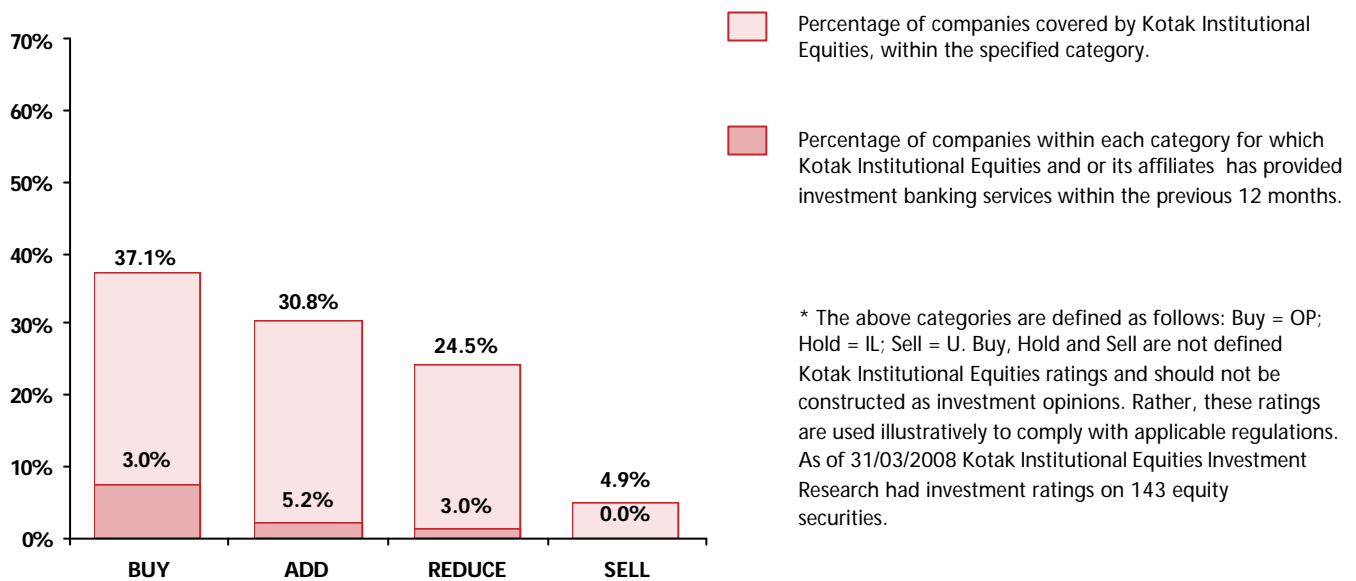
Increase in diesel price (Rs/litre)	2.00	3.00	4.00	5.00
Increase in freight rate (%)	4.3	6.5	8.6	10.8

Source: Kotak Institutional Equities estimates.

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Source: Kotak Institutional Equities.

As of March 31, 2008

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#### Old rating system

Definitions of ratings

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