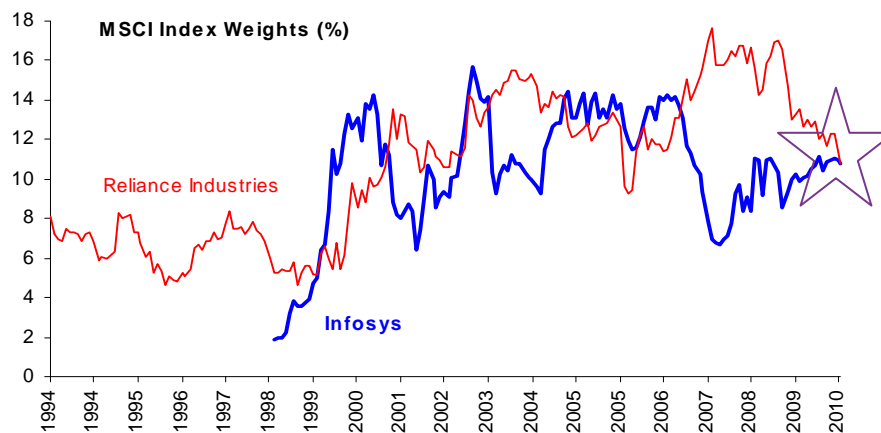


August 13, 2010

## India Strategy

### *A Tale of Two Stocks*

#### Stock Weight in MSCI India: RIL and INFY Converge



Source: FactSet, MSCI, Morgan Stanley Research

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India

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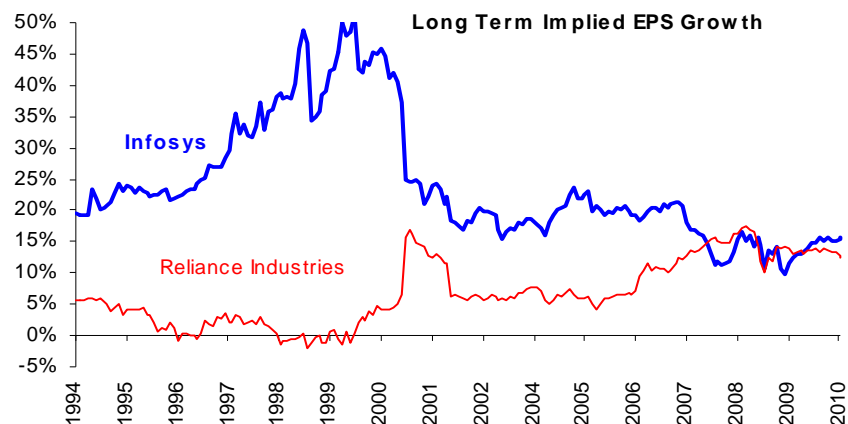
## A Tale of Two Stocks

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- **Key Debate:** Reliance Industries' MSCI India index weight converged with Infosys' weight earlier this week. In our view, this is significant because it was only at the end of 2007 when the stocks were separated by 11% points in terms of index weight with Reliance at about 17% and Infosys below 7%. They are both now at just below 11%. What is also significant is that Morgan Stanley's analysts rate both these stocks Equal-weight, that is almost 22% of the index accounted for by two stocks expected to move in line with the index. We see these noteworthy developments especially given that both companies are in some way linked to global growth and in other ways are solid proxies on India's long-term growth story. The key debate is what lies in store ahead, where are these stocks in terms of what the market is pricing in and what is the market view on these stocks?
  - **Infosys is pricing in slightly more growth than Reliance but Reliance finds greater favor with investors:**
    - Infosys has handsomely outperformed Reliance since the beginning of 2008 (by 110% points).
    - Infosys (Rs2,778.60) has gone through a big earnings and stock rating upgrade cycle since May 2009. For the first time (since we have data going back ten years) the sell side is rating Reliance (Rs972.25) below the market average. The earnings estimates have been recently cut by the sell-side consensus for RIL along with its stock rating.
    - That said, institutional investors have been buying Reliance over Infosys over the past five quarters. This is especially true for domestic institutions who have purchased Reliance and sold Infosys since March 2009.
    - Both companies have gone through a weak patch, fundamentally speaking, with ROEs dipping below trend line. The prospective estimates suggest a recovery with RIL expected to beat INFY on earnings growth (3-year CAGR of 23% vs. 18%).
    - Our single stage implied growth model suggests that the market is implying INFY's long-term EPS growth to be 15.2% vs. 12.2% for RIL. Thus, RIL is a tad more attractively valued although this has to be seen in the context of its cyclical business mix.
  - **Conclusion:** Both these stocks appear to be set for a period of consolidation relative to the market and maybe even some downside. On a five-year basis, both stocks represent high quality investments though from a top-down perspective we think the scales are tilted slightly in favor of RIL given valuations and earnings growth prospects. Investors with a 12-month horizon could be better off in more attractive large cap stocks such as SBI (Rs2784), DLF (Rs315.75), L&T (Rs1804.80), Adani Power (Rs141.30), Ranbaxy (Rs445.20) and Bharti (Rs317.55) – all rated OW.
-

## Valuations: RIL Appears Slightly More Attractively Valued

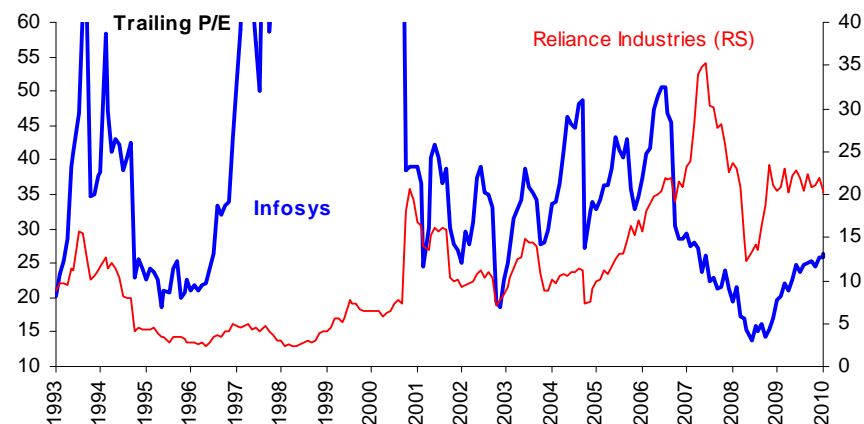
### Valuations: RIL Slightly More Attractive Than INFY



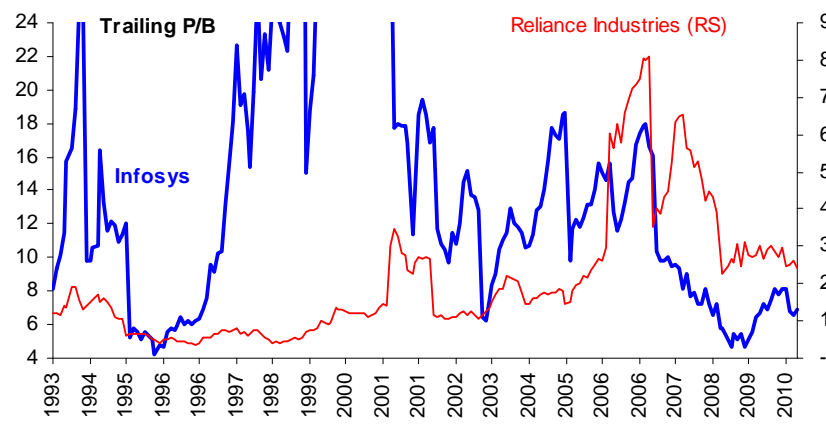
### INFY vs. RIL: Faster Growth Expected for RIL

	Infosys	Reliance
3Year EPS CAGR F10-F13	18%	23%
F10 P/E	25.5	19.6
F10 P/B	6.9	2.3
F10 ROE	27%	12%
F12E ROE	24%	14%
MSCI Index Weight (FF)	10.8%	10.8%
Market Cap (US\$ mn)	34,125	68,253
Free Float Mkt Cap (US\$ mn)	27,300	27,301
F10 Revenue (US\$ mn)	4,804	40,524

### Valuations Appear Fair Relative to History



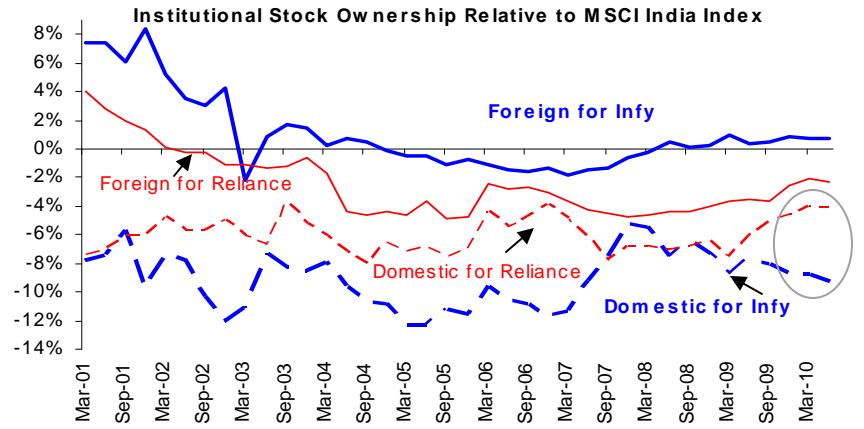
### INFY & RIL Have Suffered Some De-rating



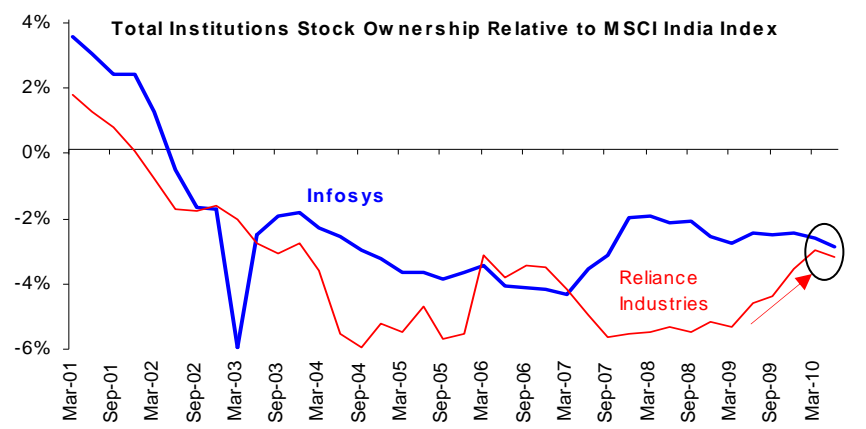
Source: FactSet, MSCI, Company Data, Morgan Stanley Research

## Consensus Views: Sell-Side Dislikes RIL vs. INFY, Buy Side Has Preferred RIL

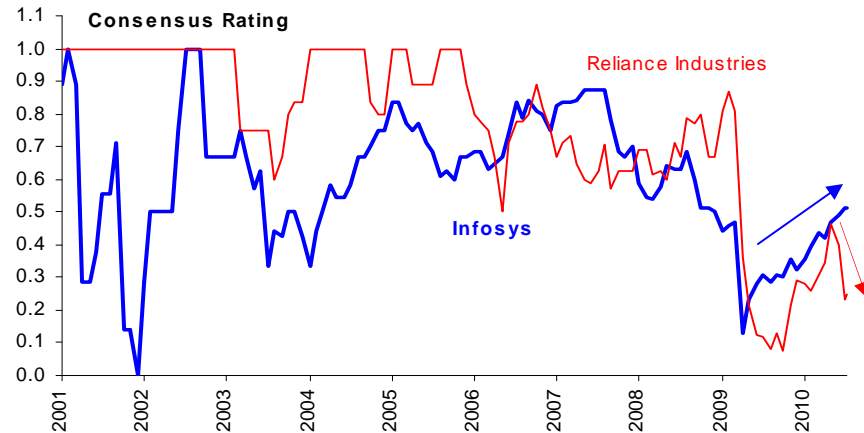
### Institutions Have Bought RIL, Domestic Inst. Sell INFY



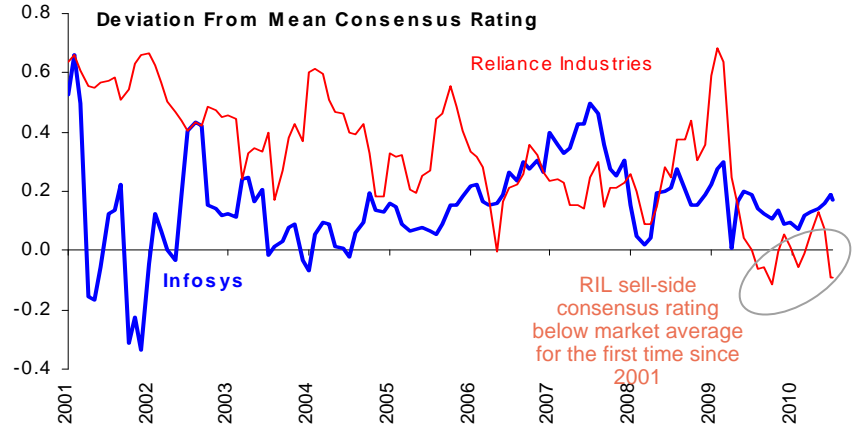
### Total Institutions: Are They Giving Up on RIL?



### Sell-Side Consensus Rating: RIL Downgraded, INFY Upgraded



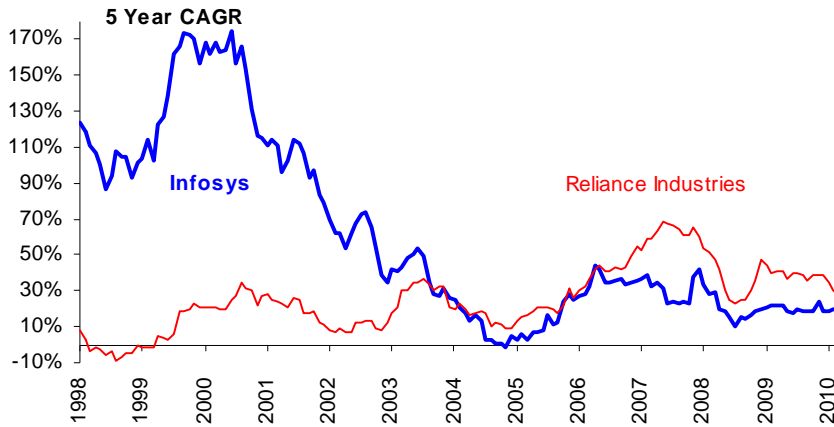
### Sell-Side Consensus Rating: RIL Below Market Average for the First Time in a Decade



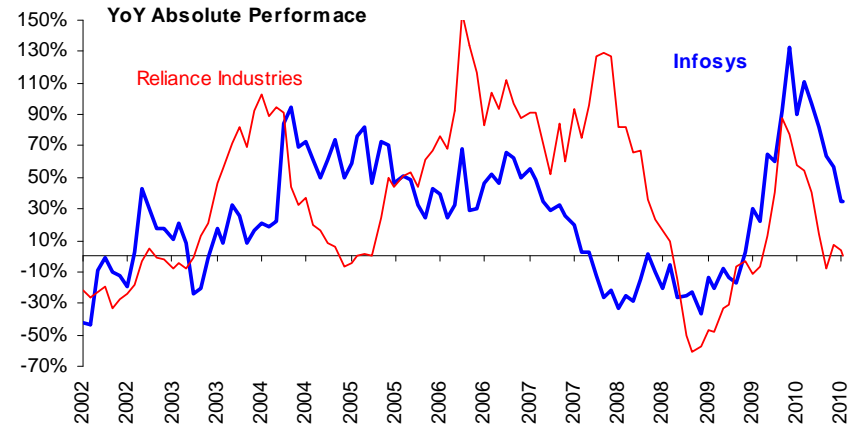
Source: Factset, IBES, MSCI, BSE, NSE, Morgan Stanley Research

# Performance: INFY Beats RIL More Recently Though RIL Has been a Long-term Winner

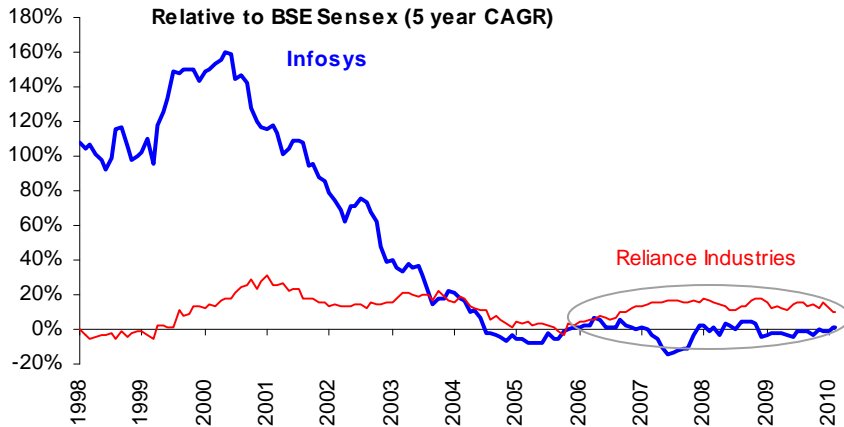
**Cumulatively RIL beats INFY by 126ppts Over 5-years**



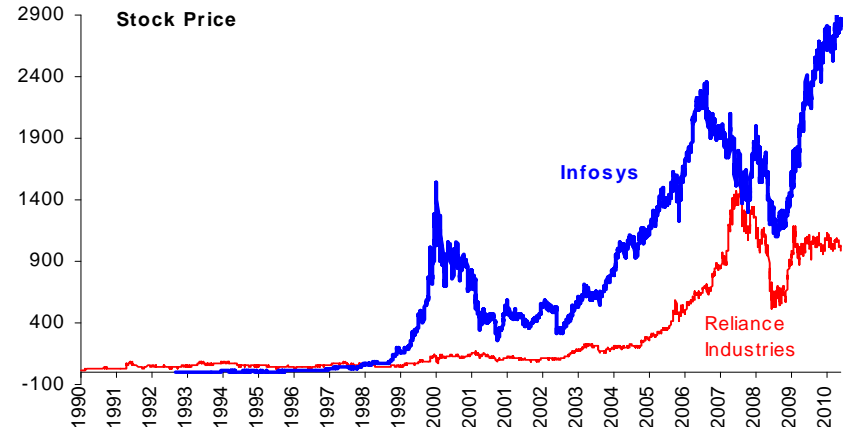
**INFY beats RIL by 35ppts in the past 12-months**



**RIL Has Outperformed the Market**



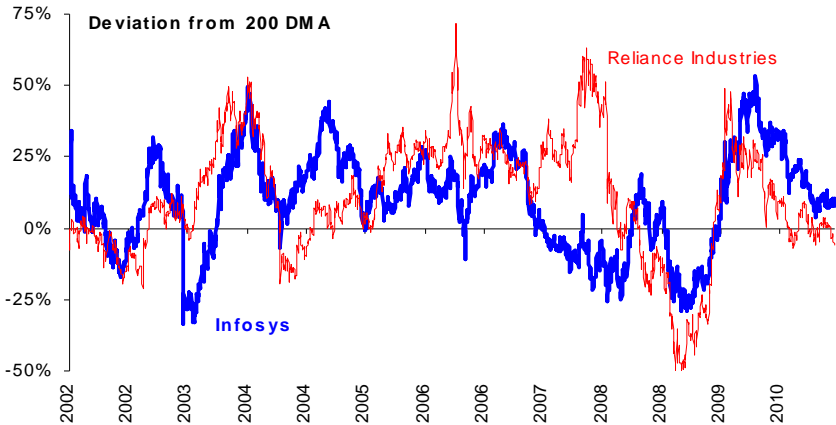
**INFY at Record Levels**



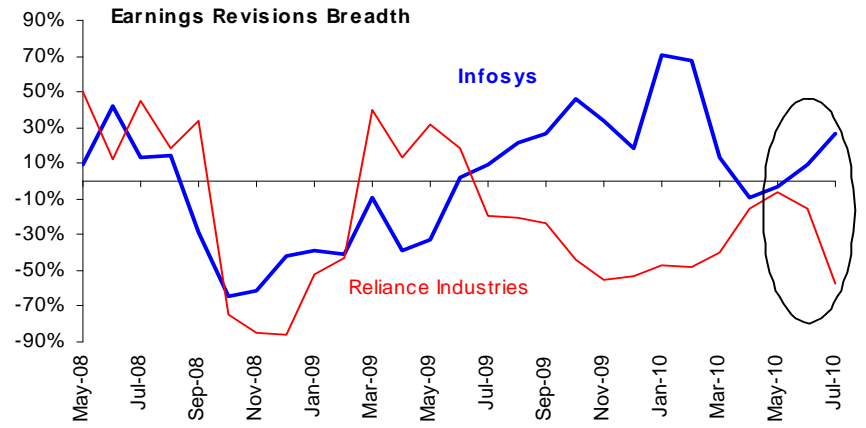
Source: Bloomberg, Morgan Stanley Research

## Momentum Indicators: RIL Losing Earnings and Price Momentum

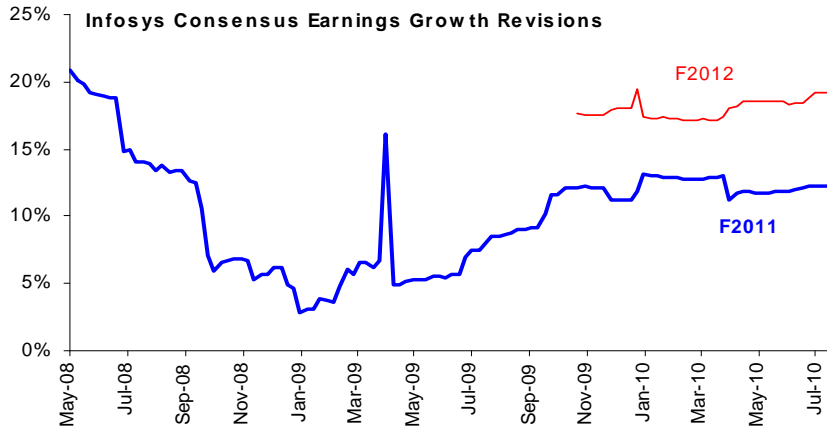
### RIL has Weaker Price Momentum



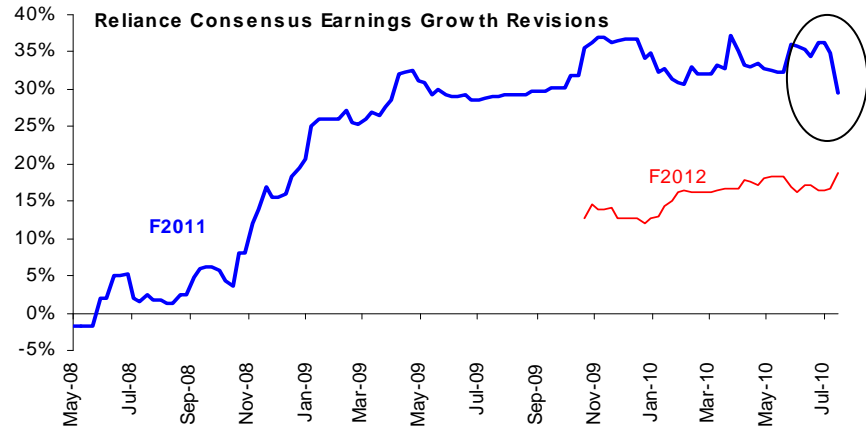
### RIL's Earnings Revisions Breadth Has Collapsed



### INFY Earnings Growth Estimates: Steady Numbers



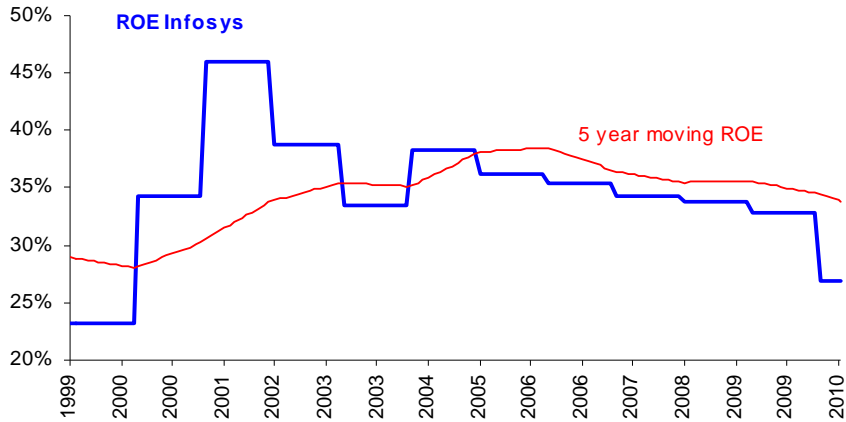
### RIL Earnings Growth Estimates: Falls Recently



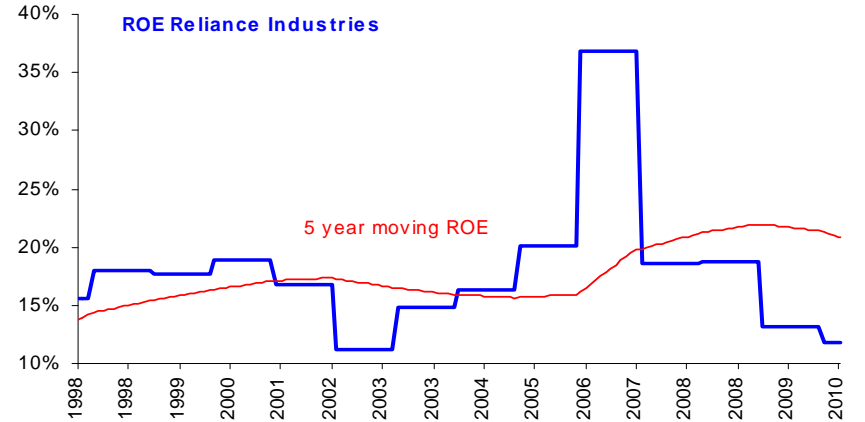
Source: Factset, IBES, Bloomberg, Morgan Stanley Research

## Fundamentals: Weaker for Both Companies

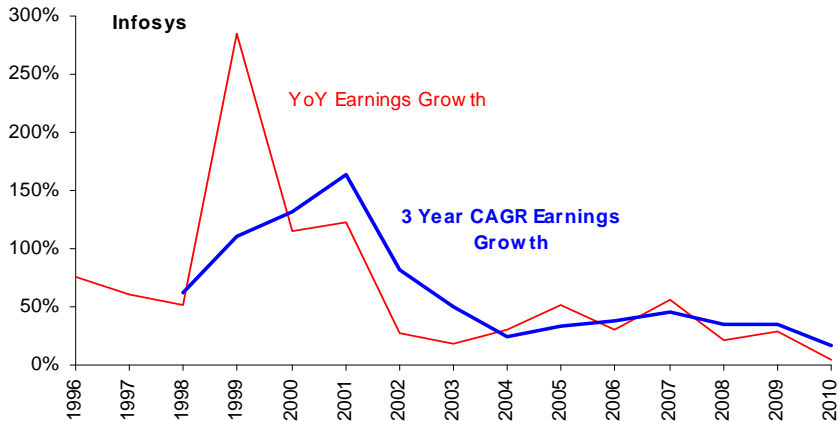
### INFY ROE: Well Below Trailing Average



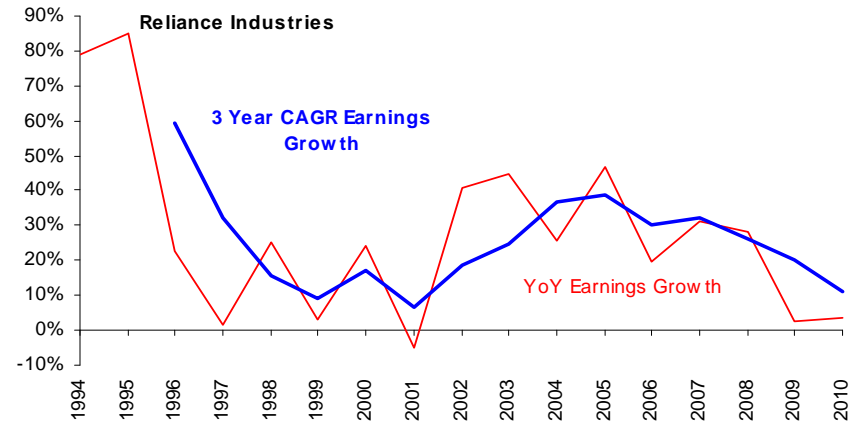
### RIL ROE: Close to 15-year Low



### INFY Earnings Growth: Some Acceleration Likely



### RIL Earnings Growth: Expected to Accelerate



Source: Company Data, Morgan Stanley Research



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	Count	% of Total	Count	% of Total IBC	% of Rating Category
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<b>Not-Rated/Hold</b>	<b>14</b>	<b>1%</b>	<b>4</b>	<b>0%</b>	<b>29%</b>
<b>Underweight/Sell</b>	<b>362</b>	<b>14%</b>	<b>93</b>	<b>11%</b>	<b>26%</b>
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