NOMURA

September 10, 2009

India
Software & IT Services

HCL Technologies (HCLT.NS - INR 308.30) Buy

Recommendation Change

Growth story to continue; upgrade to BUY

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Investment Conclusion

- We upgrade HCL Tech to BUY from Neutral and increase our price target to INR389.

Summary

- We upgrade HCL Tech to BUY from Neutral as we believe the strong growth delivered this quarter is likely to continue in the next few quarters.
- Although deal flow has been soft this quarter, our view is that HCL, with Axon, is in a position to win more deals as the global economy improves.
- Also, the order backlog of more than US$2bn should continue to provide q-q volume growth in the next few quarters.
- Margins have improved this quarter and we believe the company has done a good job in managing the Axon acquisition.
- We have raised our US dollar revenue growth forecasts in the near term and our margin assumptions.
- Our EPS estimates for FY10E and FY11E have increased by 53.4% and 64.4%, respectively due to better margins and a lower tax rate in FY11E.
- Our 12-month DCF based price target is now INR389, which implies potential upside of 26.2%.

FY Jun	2008A	2009E		2010E		2011E	
Currency INR	Actual	Old	New	Old	New	Old	New
Sales	75	103	106	104	116	114	132
OP (bn)	17	22	23	20	26	22	28
NP (bn)	10	11	13	9	14	12	19
EPS	16.7	16.7	19.1	13.6	20.9	16.8	27.6
PER (x)	18.5	18.1	16.2	22.2	14.8	18.0	11.2
EV/Sales (x)	2.9	N/A	2.0	N/A	1.9	N/A	1.6
EV/EBITDA (x)	13.1	N/A	9.3	N/A	8.5	N/A	7.6

Market Data

Market Cap (mn)	206529
Market Cap (US$ mn)	3852
Shares Outstanding (mn)	670.3
6mth Daily T/O (US$ mn)	0.88
Free float (%)	28.82
Share per ADR	N/A

Financial Summary

Proj 5-Yr EPS Grth(%)	N/A
ROE FY08 (%)	24.2
Shareholders' Equity (%)	38.4
Dividend Yield (%)	2.86

Stock Rating

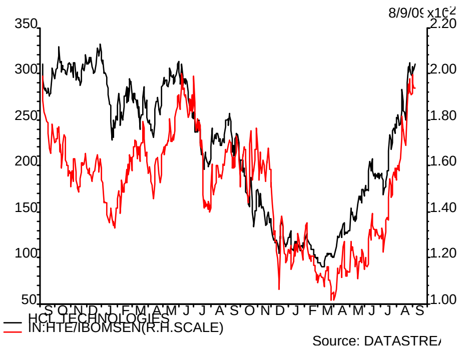
New: Buy
Old: Neutral

Target Price

New: INR 389.00
Old: INR 187.00

Sector View: Neutral

Stock Overview



Reuters	HCLT.NS
Bloomberg	HCLT IN
ADR	

Performance	1M	3M	12M
Absolute %	22.6	71.6	25.9
Rel. Market %	21.2	54.3	17.9
Rel. Sector %	N/A	N/A	N/A

52 Week Range 282.00 - 89.70

Upgrade to BUY on good results

We upgrade HCL Tech on better-than-expected revenue and margin performance during the quarter.

1. 2.7% q-q volume growth during the quarter was broad-based — across financial services, manufacturing, media and publishing, and telecom verticals. BFSI and manufacturing, which together contribute 55% of revenue, contributed almost 70% of incremental US dollar revenues during the quarter. Also, deals that were signed in the first three quarters of FY09 have started to ramp up at a fast clip.

2. The fall in EAS revenues (which contributes 23.6% of revenues) was only 0.7%, which was better than we had expected. The company was able to make up for the cut in ERP spend in the energy and utilities and public sector (which declined by 12.8% q-q on constant currency) by growth in other clients in this service line.

3. Currently HCL Tech trades at 13.8x one-year forward P/E, which is a 33.5% discount to Infosys. We value HCL based on DCF and our 12-month price target is now INR389. The increase in price target is mainly due to higher medium-term revenue and margin assumptions. Our price target translates into 14x one-year forward EPS. This is still at a 30% discount to our target price implied multiple for Infosys. Our previous price target of INR187 was based on DCF using a discount rate of 11%.

PLEASE SEE ANALYST(S) CERTIFICATION(S) ON PAGE 8 AND IMPORTANT DISCLOSURES BEGINNING ON PAGE 9

Strong growth to continue

In our view, the q-q volume growth story is likely to continue in the next few quarters owing to the following factors:

1. The company had won deals close to US$2.5bn in the past two years, of which around US$460mn in revenue is expected to come in FY10E, according to management. Some deal ramp-ups have started during the quarter and are likely to continue going forward.
2. The company's large BFS accounts such as Deutsche Bank and Lloyds Bank, which had significantly reduced IT spend in the past few quarters have begun to look at new offshoring programmes now. As per our channel checks, HCL Tech is likely to benefit from the ongoing integration project at Lloyds Bank and its revenue from this account is likely to increase by US$5-10mn.
3. The worst seems to be over for the ERP spend cycle and the market is witnessing some sort of revival, according to our channel checks and our recent conversations with the Infosys Global Head of Enterprise Solutions Mr Chandra Shekar Kakal. This should provide revenue stability to HCL-Axon, which contributes almost 25% of HCL's revenues.

4Q FY09 — impressive revenue growth

HCL Tech grew 7.6% sequentially in US dollar terms with positive growth across all three business divisions — core software, infrastructure management and BPO. Management attributed the strong growth partly to an increase in the number of billing days during the quarter and partly to a cross currency benefit due to dollar depreciation against the British pound sterling and the Euro.

Core software, which contributes 73% of revenues, grew 4.4% sequentially in US dollar terms, while BPO, which forms 10% of revenues, grew 3.9%. The strongest growth was in infrastructure management, at 25.4% in US dollar terms.

For FY09, close to US$250mn of revenue came from the US$1bn worth of deals signed during FY08 and US$1.5bn worth of deals signed during the first nine months of FY09. The combined contribution from these deals will be around US$460mn for FY10E, according to management.

Exhibit 1: HCL Tech 4Q FY09 performance by division

Performance by division (INR terms)	Q4FY08	Q3FY09	Q4FY09
Core Software			
EBITDA margin (%)	23.7	22.0	23.8
QoQ growth (%)			
Gross Revenue	12.6	21.1	(1.3)
EBITDA	18.2	8.1	6.5
Infrastructure Management Services			
EBITDA margin (%)	18.8	21.9	19.3
QoQ growth (%)			
Gross Revenue	15.0	5.2	18.5
EBITDA	19.9	18.0	4.6
BPO			
EBITDA margin (%)	28.1	15.4	15.0
QoQ growth (%)			
Gross Revenue	8.2	-7.7	-1.8
EBITDA	16.2	1.8	-4.4

Source: Company data, Nomura research

EBITDA margin improvement of 80bp

Core software EBITDA margins improved by 180bp, driven by a reduction in both direct costs and SG&A. Direct costs reduced due to a reduction in headcount by 538. SG&A expenses declined only marginally.

In the infrastructure business, while revenues increased by 25.4%, gross profit margins declined by 230bp, which management attributed to a higher onsite mix of employees and accelerated pace of investments in new delivery centres and the recently acquired New Jersey data centre.

Overall, the impact has been positive at the EBITDA level, which registered an 80bp improvement. We believe that while hiring-on-demand has helped reduce costs, once volume growth picks up hiring will accelerate and margins will also come under pressure. In the near term, however, HCL Tech will be able to maintain margins around current levels.

Lower forex losses

Forex losses were lower at US$18.5mn this quarter as against US$39.8mn in the previous quarter due to the appreciation of the INR against the USD. Going forward, management commented that US$127mn of losses in other comprehensive income (OCI) would flow to the income statement in the next four quarters which includes US$47mn of losses due to cancelled hedge covers.

The outstanding hedge position as at the end of June quarter stood at US$813mn, which was marked-to-market at 48.83 against the Indian rupee.

Higher tax rate due to one-time provision

HCL Tech's tax rate was higher this quarter due to a one-time provision made by management with respect to a difference in interpretation of the tax ruling on earnings from SEZ units. The one-time expense of US$6.6mn increased the total income tax provision to US$19.5mn, which translates into a 22% tax rate. Management has guided for a tax rate of around 18% for FY10E and FY11E.

Debt refinanced

HCL Tech refinanced US$500mn of its total debt of US$622mn partly through a US$300mn foreign currency loan, the terms of which were not disclosed. The remaining US$200mn was placed domestically with an average interest rate of 8.4% and tenor between two and five years. In the previous quarter, HCL Tech prepaid around US$85mn of the debt.

Change of estimates

We have increased our forecast of HCL Tech's US dollar revenues for FY10E and FY11E. Also, we are assuming higher margins going forward as our earlier concerns on margin dilution on account of the Axon integration have now subsided. We have assumed US$70mn forex losses for FY10E and as per management guidance a tax rate of 18% for both FY10E and FY11E. As a result of these changes, our EPS estimates have gone up by 53.4% and 64.4% for FY10E and FY11E, respectively.

Exhibit 2: Change in estimates

	New		Old		Change (%)	
	FY10E	FY11E	FY10E	FY11E	FY10E	FY11E
Revenue (US$ mn)	$2,548	$2,934	$2,350	$2,754	8.4	6.5
Revenue (INR bn)	116	132	104	114	11.4	15.8
EBITDA margin (%)	22.1	21.5	19.4	19.2	14.3	12.2
Tax Rate (%)	18.0	18.0	19.5	27.2	-7.7	-33.8
EPS (INR)	20.9	27.6	13.6	16.8	53.4	64.4

Source: Nomura estimates

Valuation

We value HCL Tech based on DCF and our 12-month price target is now INR389. The increase in price target is due mainly to higher revenue and margin assumptions. Our price target translates into 14x one-year forward EPS. This is still at a 30% discount to our target price implied multiple for Infosys. Our DCF assumptions are as follows:

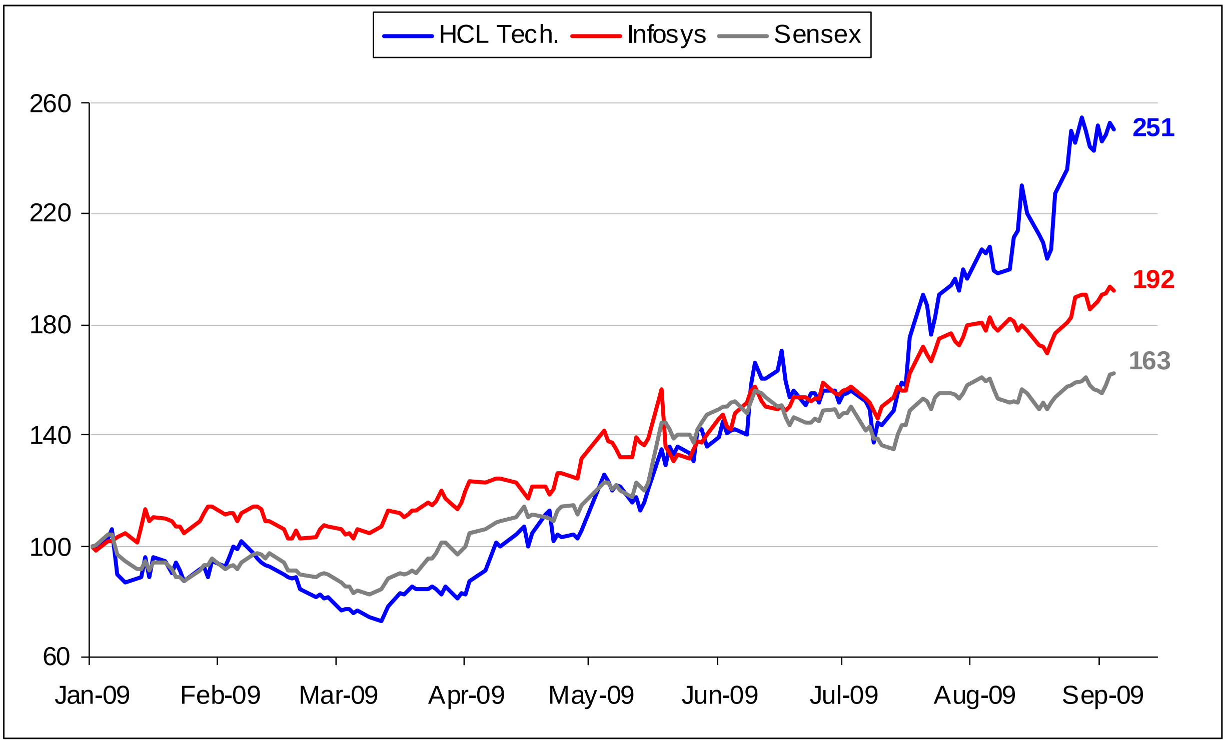
Exhibit 3: Assumptions underlying DCF valuation for HCL Tech

Growth rate in the first period	15.8%
Growth rate in the second period	13.3%
Growth rate in the third period	10.8%
Terminal growth rate	5.0%
Discount rate	11.0%
No. of years in the first period	2
No. of years in the second period	3
No. of years in the third period	5

Source: Nomura estimates

On a YTD basis, HCL Tech has outperformed both the Sensex and its peer Infosys by a wide margin, with 151% gains compared with 63% for the Sensex and 92% for Infosys.

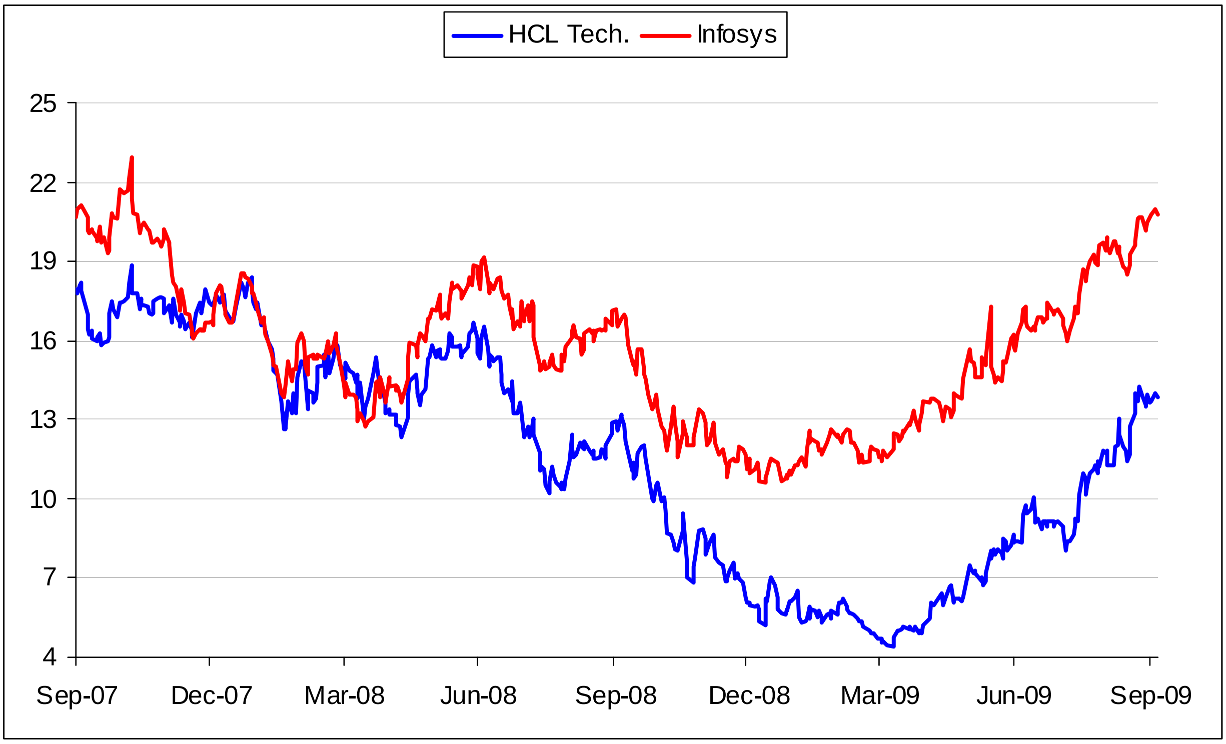
Exhibit 4: HCL Tech — stock price performance vs Infosys and Sensex



Source: Bloomberg, Nomura research

Currently HCL Tech trades at 13.8x one-year forward P/E, which is at 33.5% discount to Infosys.

Exhibit 5: HCL Tech — one-year forward P/E chart comparison with Infosys



Source: Bloomberg, Nomura research

Exhibit 6: 4Q FY09 result highlights

Consolidated quarterly results (INR mn)	**Q4FY08**	**Q3FY09**	**Q4FY09**	**Q4FY09E**
Gross Revenue	21,688	28,620	29,085	25,790
Direct Costs	12,912	18,009	18,135	16,555
Gross Profit	8,776	10,612	10,950	9,235
S,G&A	3,697	4,502	4,512	4,183
EBITDA	5,079	6,109	6,438	5,051
Depreciation & Amortization	852	1,415	1,193	1,381
EBIT	4,227	4,695	5,245	3,670
Foreign Exchange Gains (Loss)	(3,000)	(2,018)	(886)	(1,628)
Other Income, net	357	(25)	(115)	(13)
PBT	1,584	2,652	4,244	2,030
Provision for income taxes	202	487	934	315
Share from equity investment	0	0	(5)	(5)
Loss/(Income) of minority shareholders	22	15	0	(23)
Profit after tax	1,403	2,180	3,305	1,687
EPS	**1.8**	**3.3**	**4.9**	**2.5**
QoQ Growth (%)				
Revenues	12.4	14.9	1.6	(9.9)
EBITDA	18.1	9.0	5.4	(17.3)
PAT	(58.7)	(41.7)	51.6	(22.6)
YoY Growth (%)				
Revenues	34.5	48.3	34.1	18.9
EBITDA	46.3	42.1	26.8	(0.5)
PAT	(71.2)	(35.8)	135.6	20.3
Margins (%)				
Gross margin	40.5	37.1	37.6	35.8
EBITDA margin	23.4	21.3	22.1	19.6
Net margin	6.5	7.6	11.4	6.5
Tax Rate	12.8	18.4	22.0	15.5

Source: Company data, Nomura research

The strong performance in the media publishing and entertainment vertical is due to the ramp up at Readers Digest, where the company recently won a large multi-year total IT outsourcing deal.

Exhibit 7: HCL Tech — q-q growth for verticals

(%)	**4Q FY08**	**3Q FY09**	**4Q FY09**
Banking, FS & insurance (BFSI)	0.2	-6.0	13.0
Manufacturing	8.1	11.5	9.7
Telecom	1.4	-15.5	11.1
Retail	8.8	-1.1	2.9
Media publishing & entertainment (MPE)	2.1	0.3	20.5
Life sciences	7.7	17.8	9.3
Energy-utilities-public sector	0.0	206.9	-8.1

Source: Company data, Nomura research

Enterprise application services, under which Axon revenue has been integrated, grew 3.6% sequentially although infrastructure services contributed to the lion's share of overall sequential growth with 25.4% growth.

Exhibit 8: HCL Tech — q-q growth for services

(%)	4Q FY08	3Q FY09	4Q FY09
Enterprise application services	4.9	116.3	3.6
Engg and R&D services	9.2	-5.5	-5.1
Industry solutions	0.3	-4.7	12.5
Infrastructure services	6.0	1.0	25.4
BPO services	0.3	-11.0	4.3

Source: Company data, Nomura research

Asia Pacific saw strong 18.9% growth, which, according to management, was due to the partnership tie-ups that HCL had with SAP. Management commented that there was considerable potential for growth in this geography especially in newer areas like cloud computing.

Exhibit 9: HCL Tech — q-q growth for geographies

(%)	4Q FY08	3Q FY09	4Q FY09
US	6.7	12.6	3.9
Europe	2.1	12.4	11.1
Asia-Pacific	-3.3	-4.0	18.9

Source: Company data, Nomura research

Detailed financials

Exhibit 10: Income statement

Year ended 30 Jun (INRmn)	FY08	FY09	FY10E	FY11E
Net sales	74,772	106,311	115,883	132,021
Growth (%)	23.9	42.2	9.0	13.9
Operating expenses	-58,223	-82,844	-90,222	-103,590
Raw material	-45,913	-65,481	-71,950	-82,149
Power	0	0	0	0
Employee expenses	0	0	0	0
SG&A expenses	-12,310	-17,363	-18,272	-21,441
R&D expenses	0	0	0	0
Other operating expenses	0	0	0	0
Core EBITDA	16,549	23,467	25,661	28,431
Other income	-1,170	-3,672	-1,868	1,468
EBITDA	15,379	19,796	23,792	29,899
Depreciation	-2,965	-4,487	-4,939	-5,522
Expenses capitalised	0	0	0	0
EBIT	12,414	15,308	18,853	24,378
Interest paid	0	0	-1,786	-1,786
Associates	0	-10	-18	-18
Non-recurring items (net of taxes)	-813	-188	0	0
Pre-tax profit	11,600	15,111	17,049	22,573
Tax provided	-1,258	-2,544	-3,072	-4,066
Deferred tax	0	0	0	0
Profit after tax	10,343	12,567	13,977	18,507
Minority interests	-20	29	0	0
Preference dividend	0	0	0	0
Net profit	10,323	12,596	13,977	18,507
Adjusted net profit	11,136	12,784	13,977	18,507
Growth (%)	-18.5	14.8	9.3	32.4
Wtd avg shares (m)	668	670	670	670
Fully diluted shares	668	670	670	670
Dividend paid	-5,341	-4,680	-2,680	-2,680

Source: Company data, Nomura estimates

Exhibit 11: Balance sheet

Year ended 30 Jun (INRmn)	FY08	FY09	FY10E	FY11E
Cash	3,550	7,291	6,581	14,872
Investments	19,215	14,009	14,792	14,792
Current assets	49,806	56,777	59,713	74,856
Net fixed assets	11,284	15,862	17,923	20,401
Other non-current assets	6,987	53,930	61,113	66,255
Total assets	81,846	126,939	138,748	161,512
Current liabilities	25,613	32,675	33,445	39,422
Total debt	550	29,771	29,771	29,771
Other liabilities	0	7,634	7,814	9,210
Total liabilities	26,163	70,080	71,030	78,404
Share capital	1,335	1,340	1,340	1,340
Reserves & surplus	40,475	55,503	66,363	81,753
Shareholders' funds	41,810	56,843	67,703	83,093
Minorities	65	16	16	16
Total equity & liabilities	68,038	126,939	138,748	161,512

Source: Company data, Nomura estimates

Exhibit 12: Cash flow statement

Year ended 30 Jun (INRmn)	FY08	FY09	FY10E	FY11E
Pre-tax profit	12,547	15,308	17,067	22,591
Depreciation	3,032	4,487	4,939	5,522
Tax paid	-1,274	-2,544	-3,072	-4,066
Chg in working capital	-3,746	-1,595	-1,738	-2,112
Other operating activities	0	0	0	0
Cash flow from operations (a)	10,558	15,657	17,196	21,934
Capital expenditure	-3,772	-6,563	-5,927	-6,626
Chg in investments	0	-33,917	0	0
Chg in associates	0	0	0	0
Other investing activities	0	-500	0	0
Cash flow from investing (b)	-3,772	-40,980	-5,927	-6,626
Free cash flow (a+b)	6,786	-25,323	11,269	15,308
Equity raised/(repaid)	0	0	0	0
Chg in minorities	0	0	0	0
Debt raised/(repaid)	0	34,471	-3,150	-6,300
Dividend (incl. tax)	-5,853	-6,375	-5,032	-6,662
Other financing activities	0	0	0	0
Cash flow from financing (c)	-6,000	28,736	-8,182	-12,962
Net chg in cash (a+b+c)	786	3,413	3,087	2,346

Source: Company data, Nomura estimates

Exhibit 13: Key ratios

Year ended 30 Jun	FY08	FY09	FY10E	FY11E
Adjusted EPS (INR)	16.7	19.1	20.9	27.6
Adjusted EPS growth (%)	-20.3	14.4	9.3	32.4
Core EBITDA growth (%)	23.9	41.8	9.3	10.8
Core EBITDA margin (%)	22.1	22.1	22.1	21.5
Pre-tax margin (%)	15.5	14.2	14.7	17.1
ROE (%)	24.2	25.9	22.4	24.5
ROCE (%)	26.4	22.4	18.9	21.4
Net debt/equity (%)	-68.8	19.0	12.4	0.1

Source: Company data, Nomura estimates

Exhibit 14: Valuations

Year ended 30 Jun	FY08	FY09	FY10E	FY11E
PER (x)	18.5	16.2	14.8	11.2
PCE (x)	14.6	12.0	10.9	8.6
Price/book (x)	4.9	3.6	3.1	2.5
Yield (%)	2.6	2.3	1.3	1.3
EV/net sales (x)	2.9	2.0	1.9	1.6
EV/EBITDA (x)	13.1	9.3	8.5	7.6

Source: Company data, Nomura estimates

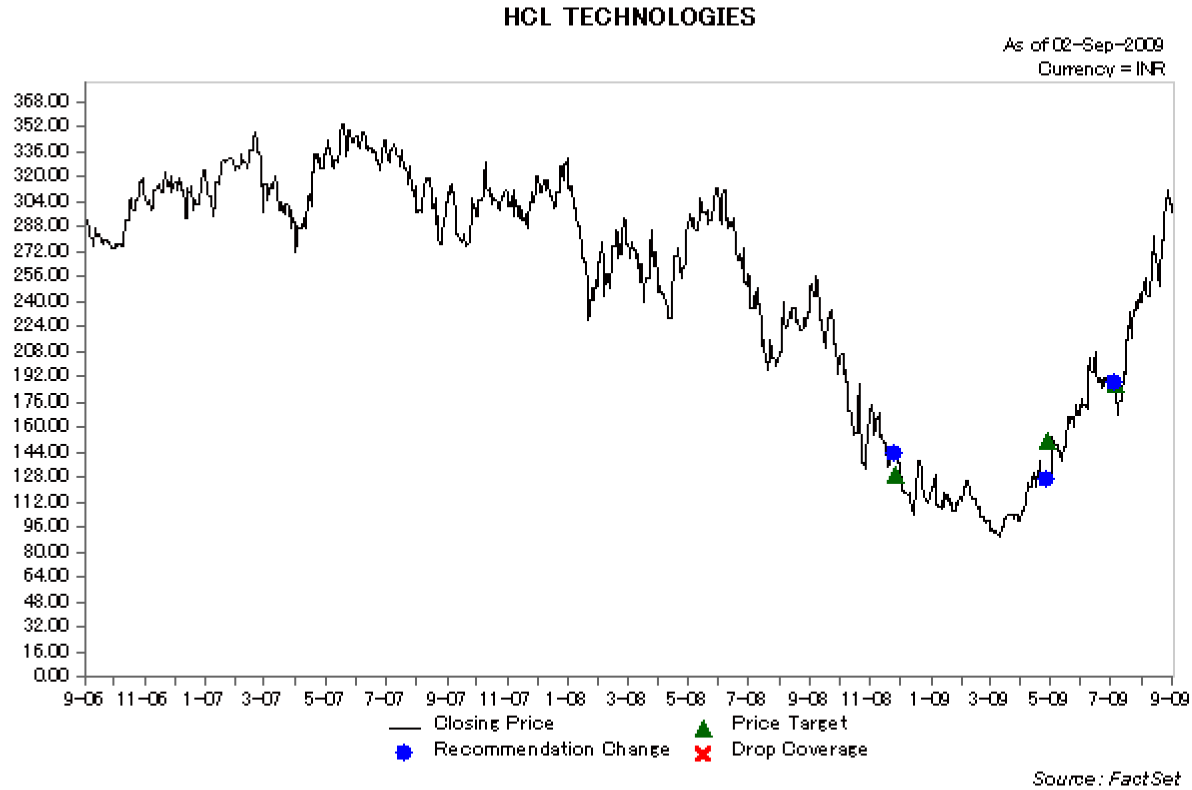
Analyst Certification:

We, Harmendra Gandhi and Pinku Pappan, hereby certify (1) that the views expressed in this Company Note accurately reflect our personal views about any or all of the subject securities or issuers referred to in this Company Note and (2) no part of our compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this Company Note.

Important Disclosures:

HCL Technologies (HCLT.NS) **INR 308.30 (08-Sep-2009)** **Buy / Neutral**

Rating and Price Target Chart:



Currency=INR

Date	Closing Price	Rating	Price Target
06-Jul-09	186.90		187.00
06-Jul-09	186.90	Neutral	
28-Apr-09	125.85		152.00

Date	Closing Price	Rating	Price Target
28-Apr-09	125.85	Buy	
26-Nov-08	143.00		130.00
26-Nov-08	143.00	Reduce	

FOR EXPLANATIONS OF RATINGS REFER TO THE STOCK RATING KEYS LOCATED ON THE PAGE FOLLOWING THE LAST PRICE CHART.

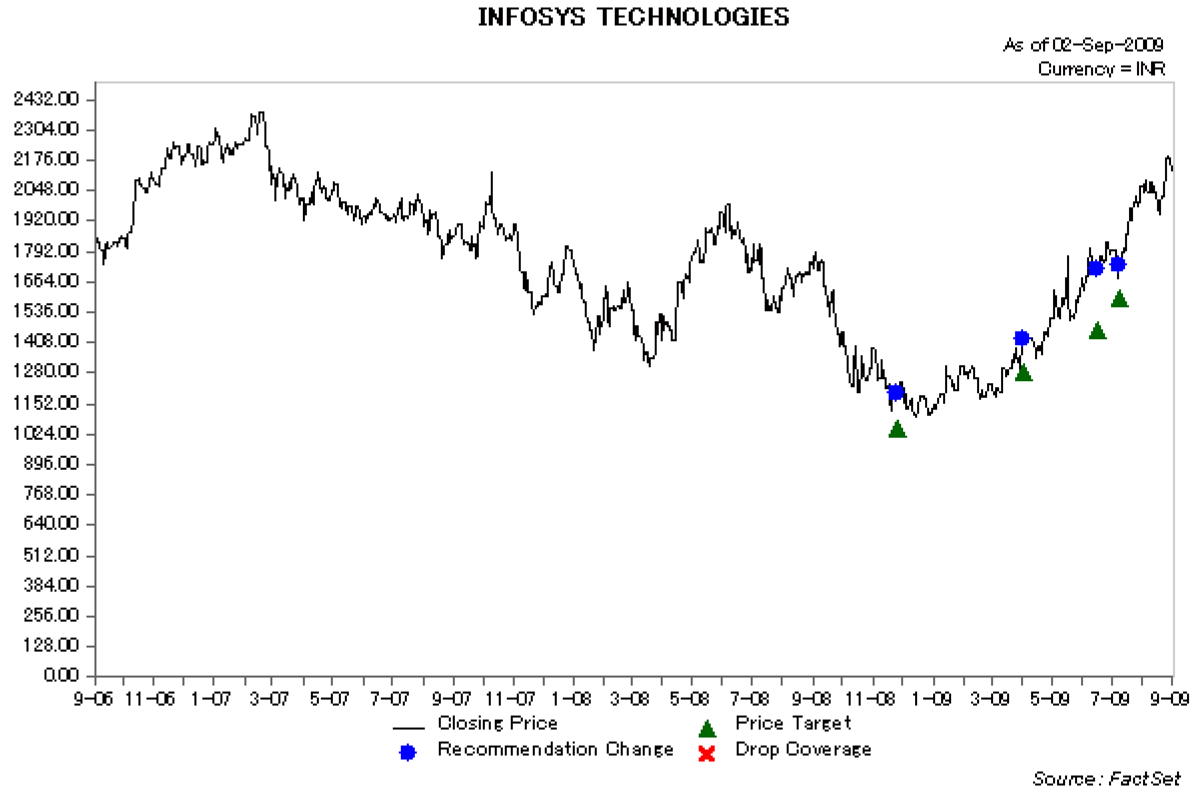
Valuation Methodology: Our DCF based price target is INR 389 and is calculated using 11% discount rate and terminal growth rate assumption of 5%. The target price of INR 389 also translates into a 14X one-year forward P/E which is a 30% discount to the target price P/E multiple for Infosys.

Risks Which May Impede the Achievement of the Price Target: There are two risks to our target price: 1) lower revenue ramp-up from the order book and 2) greater-than-expected appreciation of the rupee against the US dollar.

Important Disclosures Continued:

Infosys Technologies (INFY.NS) **INR 2200.05 (08-Sep-2009)** **Neutral / Neutral**

Rating and Price Target Chart:



Currency=INR

Date	Closing Price	Rating	Price Target
10-Jul-09	1726.50		1598.00
10-Jul-09	1726.50	Reduce	
17-Jun-09	1710.50		1458.00
17-Jun-09	1710.50	Reduce	

Date	Closing Price	Rating	Price Target
03-Apr-09	1420.40		1283.00
03-Apr-09	1420.40	Reduce	
26-Nov-08	1187.25		1049.00
26-Nov-08	1187.25	Reduce	

FOR EXPLANATIONS OF RATINGS REFER TO THE STOCK RATING KEYS LOCATED ON THE PAGE FOLLOWING THE LAST PRICE CHART.

Valuation Methodology: Our 12-month price target of INR2,271 is based on a DCF calculation, assuming a terminal growth rate of 5% and a 11% cost of equity in rupee terms for Indian software companies.

Risks Which May Impede the Achievement of the Price Target: There are two risks to our target price: 1) appreciation of the rupee against the dollar more than what we expect and 2) a double dip recession

Important Disclosures Continued:

Company Name	Ticker	Price	Price Date	Stock / Sector Rating
HCL Technologies	HCLT.NS	INR 308.30	08-Sep-2009	Buy / Neutral

Mentioned Company	Ticker	Price	Price Date	Stock / Sector Rating
Infosys Technologies	INFY.NS	INR 2200.05	08 Sep 2009	Neutral / Neutral

All share prices mentioned are closing prices unless otherwise stated.

ISSUER SPECIFIC REGULATORY DISCLOSURES

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As at 30 June 2009.

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The rating system is a relative system indicating expected performance against a specific benchmark identified for each individual stock. Analysts may also indicate absolute upside to price target defined as (fair value - current price)/current price, subject to limited management discretion. In most cases, the fair value will equal the analyst's assessment of the current intrinsic fair value of the stock using an appropriate valuation methodology such as discounted cash flow or multiple analysis, etc.

Stocks:

• A rating of "1", or **"Buy"**, indicates that the analyst expects the stock to outperform the Benchmark over the next 12 months.
• A rating of "2", or **"Neutral"**, indicates that the analyst expects the stock to perform in line with the Benchmark over the next 12 months.
• A rating of "3", or **"Reduce"**, indicates that the analyst expects the stock to underperform the Benchmark over the next 12 months.
• A rating of **"RS-Rating Suspended"** indicates that the rating and target price have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including when Nomura is acting in an advisory capacity in a merger or strategic transaction involving the company.

Benchmarks are as follows: **United States:** S&P 500, MSCI World Technology Hardware & Equipment; **Europe:** Please see valuation methodologies for explanations of relevant benchmarks for stocks (accessible through the left hand side of the Nomura Disclosure web page: http://www.nomura.com/research); **Global Emerging Markets (ex-Asia):** MSCI Emerging Markets ex-Asia.

Sectors:

A **"Bullish"** stance, indicates that the analyst expects the sector to outperform the Benchmark during the next 12 months.
A **"Neutral"** stance, indicates that the analyst expects the sector to perform in line with the Benchmark during the next 12 months.
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Explanation of Nomura's equity research rating system for Asian companies under coverage ex Japan published from 30 October 2008 and in Japan from 6 January 2009:

Stocks:

Stock recommendations are based on absolute valuation upside (downside), which is defined as (Price Target – Current Price) / Current Price, subject to limited management discretion. In most cases, the Price Target will equal the analyst's 12-month intrinsic valuation of the stock, based on an appropriate valuation methodology such as discounted cash flow, multiple analysis, etc.

• A rating of "1", or "**Buy**" recommendation indicates that potential upside is 15% or more.
• A rating of "2", or "**Neutral**" recommendation indicates that potential upside is less than 15% or downside is less than 5%.
• A rating of "3", or "**Reduce**" recommendation indicates that potential downside is 5% or more.
• A rating of "**RS**" or "**Rating Suspended**" indicates that the rating and target price have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including when Nomura is acting in an advisory capacity in a merger or strategic transaction involving the subject company.
• Stocks labeled as "**Not rated**" or shown as "**No rating**" are not in Nomura's regular research coverage.

Sectors:

A "**Bullish**" rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a positive absolute recommendation.
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A "**Bearish**" rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a negative absolute recommendation.

Explanation of Nomura's equity research rating system in Japan published prior to 6 January 2009 (and ratings in Europe, Middle East and Africa, US and Latin America published prior to 27 October 2008):

Stocks:

• A rating of "1", or **"Strong buy"**, indicates that the analyst expects the stock to outperform the Benchmark by 15% or more over the next six months.
• A rating of "2", or **"Buy"**, indicates that the analyst expects the stock to outperform the Benchmark by 5% or more but less than 15% over the next six months.
• A rating of "3", or **"Neutral"**, indicates that the analyst expects the stock to either outperform or underperform the Benchmark by less than 5% over the next six months.
• A rating of "4", or **"Reduce"**, indicates that the analyst expects the stock to underperform the Benchmark by 5% or more but less than 15% over the next six months.
• A rating of "5", or **"Sell"**, indicates that the analyst expects the stock to underperform the Benchmark by 15% or more over the next six months.
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Benchmarks are as follows: **Japan**: TOPIX; **United States**: S&P 500, MSCI World Technology Hardware & Equipment; **Europe**, by sector — *Hardware/Semiconductors*: FTSE W Europe IT Hardware; *Telecoms*: FTSE W Europe Business Services; *Business Services*: FTSE W Europe; *Auto & Components*: FTSE W Europe Auto & Parts; *Communications equipment*: FTSE W Europe IT Hardware; **Ecology Focus:** Bloomberg World Energy Alternate Sources; **Global Emerging Markets:** MSCI Emerging Markets ex-Asia.

Explanation of Nomura's equity research rating system for Asian companies under coverage ex Japan published prior to 30 October 2008:

Stocks:

Stock recommendations are based on absolute valuation upside (downside), which is defined as (Fair Value - Current Price)/Current Price, subject to limited management discretion. In most cases, the Fair Value will equal the analyst's assessment of the current intrinsic fair value of the stock using an appropriate valuation methodology such as Discounted Cash Flow or Multiple analysis etc. However, if the analyst doesn't think the market will revalue the stock over the specified time horizon due to a lack of events or catalysts, then the fair value may differ from the intrinsic fair value. In most cases, therefore, our recommendation is an assessment of the difference between current market price and our estimate of current intrinsic fair value. Recommendations are set with a 6-12 month horizon unless specified otherwise. Accordingly, within this horizon, price volatility may cause the actual upside or downside based on the prevailing market price to differ from the upside or downside implied by the recommendation.

• A rating of "1", or "**Strong buy**" recommendation indicates that upside is more than 20%.
• A rating of "2", or "**Buy**" recommendation indicates that upside is between 10% and 20%.
• A rating of "3", or "**Neutral**" recommendation indicates that upside or downside is less than 10%.
• A rating of "4", or "**Reduce**" recommendation indicates that downside is between 10% and 20%.
• A rating of "5", or "**Sell**" recommendation indicates that downside is more than 20%.

Sectors:

A "**Bullish**" rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a positive absolute recommendation.
A "**Neutral**" rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a neutral absolute recommendation.
A "**Bearish**" rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a negative absolute recommendation.

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