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### News Roundup

#### Corporate

- DLF Ltd's mega initial share sale got bids for 78 per cent of the shares on offer on the opening day of the issue. Foreign investors bid for 120.01 mn shares out of the 104.4 mn shares reserved for qualified institutional buyers (QIBs), while domestic financial institutions submitted bids for 13.36 mn shares. (BS)
- Reliance industries (RILs) process of inviting price and volume bids from potential customers along the pipeline route are likely to be seen in conformity with the prescribed guidelines of the government on natural gas pricing. (ET)
- The Tata-Changi airport consortium has bid for the development of three airports in Karnataka. The consortium is also bidding for upcoming airports at Navi Mumbai and Greater Noida near New Delhi. (BS)

#### Economic and political

- The government is likely to review fuel prices in mid-July, as the same have not been changed since February. (ET)
- Growth in the six-sector infrastructure index leveled off at 7.4% in April 2007 against a 7.3% growth in April 2006. The overall performance was hurt by the weak performance of cement, coal and finished steel. (FE)

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

### EQUITY MARKETS

India	Change, %			
	11-Jun	1-day	1-mo	3-mo
Sensex	14,083	0.1	2.1	9.2
Nifty	4,146	0.0	1.7	11.0
<b>Global/Regional indices</b>				
Dow Jones	13,425	0.0	0.7	9.0
Nasdaq Composite	2,572	(0.1)	0.4	7.1
FTSE	6,568	1.0	0.0	5.4
Nikkei	17,770	(0.4)	1.2	2.8
Hang Seng	20,535	(0.4)	0.3	5.6
KOSPI	1,723	0.4	7.4	19.5
<b>Value traded - India</b>				
		Moving avg, Rs bn		
	11-Jun	1-mo	3-mo	
Cash (NSE+BSE)	110.8	#####	#####	
Derivatives (NSE)	289.4	387.0	349.4	
Deri. open interest	631.1	534.5	543.1	

#### Forex/money market

	Change, basis points			
	11-Jun	1-day	1-mo	3-mo
Rs/US\$	40.8	-	(6)	(341)
6mo fwd prem, %	0.7	(25)	71	24
10yr govt bond, %	8.3	11	14	24

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

	8-Jun	MTD	CYTD
FIs	(222)	1,257	40
MFs	56	240	(303)

#### Top movers -3mo basis

Best performers	Change, %			
	11-Jun	1-day	1-mo	3-mo
Balaji Telefilms	220	(1.6)	22.7	96.1
Reliance Cap	958	(0.6)	21.3	52.1
GESCO	290	1.1	11.5	46.6
Moser Baer	435	(4.3)	14.4	39.7
SBI	1,340	(1.3)	16.6	37.2
<b>Worst performers</b>				
Bajaj Auto	2,119	(0.1)	(22.1)	(15.6)
United Phos	271	(0.7)	(9.1)	(15.0)
Tata Motors	652	(0.3)	(8.9)	(14.7)
Ashok Leyland	36	0.8	(3.4)	(11.8)
Cipla	211	(0.2)	3.1	(9.2)

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**Chemicals****RELI.BO, Rs1668**

Rating	U
Sector coverage view	Neutral
Target Price (Rs)	1,400
52W High -Low (Rs)	1785 - 843
Market Cap (Rs bn)	2,324

**Financials**

March y/e	2007	2008E	2009E
Sales (Rs bn)	1,052	957	1,146
Net Profit (Rs bn)	107.2	96.4	140.5
EPS (Rs)	76.9	71.5	98.5
EPS gth	21.8	(7.0)	37.6
P/E (x)	21.7	23.3	16.9
EV/EBITDA (x)	12.7	13.5	8.7
Div yield (%)	0.7	0.7	0.8

**Shareholding, March 2007**

	% of		Over/(under)
	Pattern	Portfolio	weight
Promoters	43.5	-	-
FIs	23.1	7.4	0.7
MFs	2.5	4.9	(1.9)
UTI	-	-	(6.7)
LIC	4.5	7.9	1.2

**Reliance Industries: More details on KG D-6 gas pricing—a complex formula for a straightforward price objective**

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- **Smart pricing formula designed to insulate price against exchange rate and crude oil price movements**
- **Acceptance by the government and new users is another issue though**
- **We will await for government approval, industry feedback and pending disputes with NTPC and RNRL before reviewing our pricing assumptions**

After examining the formula for gas pricing proposed by Reliance available on a paid website, which presumably gives the correct one (none of the newspapers have carried the formula), our conclusions remain unchanged. The formula is linked to exchange rate and crude oil price apart from a constant factor and will result in gas price between US\$4/mn BTU and US\$5/mn BTU in most cases. We doubt new power projects would find the pricing of KG D-6 gas competitive versus domestic coal. Also, press reports have quoted government officials commenting on the appropriateness of a price determination based on 10 participants. The bids are in the range of US\$4.64-4.86/mn BTU (wellhead) based on the proposed formula. Finally, we would watch for resolution of Reliance's pending legal dispute with RNRL. We retain our 12-month fair valuation of Rs1,400 based on 9X FY2010E EPS discounted to June 2008. Key upside risks stem from continued high global liquidity and new E&P discoveries.

**Smart formula designed to insulate against adverse exchange rate and crude oil price movements.** The proposed formula appears to be designed to protect Reliance against adverse exchange rate movement (appreciation in the rupee) or crude oil price movements. In fact, our analysis (see Exhibits 1 and 2 for details of formula and sensitivity of price to variables) suggests that the price of gas (in both US Dollar and rupee terms) will be in a relatively tight band despite a large band of crude oil price (US\$25/bbl and US\$65/bbl) and potential wide variation in rupee-dollar exchange rates.

**We are comfortable with our estimate of US\$4/mn BTU for KG D-6 gas price currently.** We note that our assumed US\$4/mn BTU price for KG D-6 gas at Rs43/US\$ translates into around US\$4.2/mn BTU at Rs41/US\$. We will wait for the government's approval and industry acceptance of the formula before reviewing our price and earnings assumptions. Also, we note that Reliance would still need to supply 11 mcm/d of gas to NTPC at US\$2.47/mn BTU irrespective of the current proposed formula; this would pull down the blended price.

**Several issues about the formula and without the formula.** We would be curious to see the government's response to Reliance's attempt to fix a market price (competitive bidding) through a limited tender to five extant power producers and fertilizer producers each. We are even more curious to see the outcome of Reliance's ongoing dispute with RNRL; we find it odd that Reliance is discussing volumes with other players without clarity on its disputes with RRNL and NTPC.

**We would be surprised if new units accept the formula or gas at the formula price.** We would be surprised to see new power plant developers accepting the formula or in fact using gas as a fuel at the proposed formula-based prices. At US\$50/bbl crude price (normalized Dated Brent) and Rs40/US\$, we compute the price of gas at US\$4.46/mn BTU, which would result in significantly higher cost of power generation versus a coal-based power plant. Also, we assume a power developer would like to have some clarity on the quantity of gas and price of its fuel longer-term rather be exposed to both volume and price uncertainties. We note that the constant factor in the formula is valid for three years (until March 31, 2012); this would presumably suggest that gas pricing can change in the future.

As highlighted in our previous note, we are surprised to see a LNG-type pricing formula for domestic gas. We are not sure whether domestic gas pricing should be based on crude oil and on a complicated formula linked to exchange rate and crude prices.

### Formula designed to keep pricing in a narrow band in rupee terms

Selling price of gas from KG D-6 block at various levels of crude price and exchange rate (US\$/mn BTU)

$$\text{Selling price} = 112.5 \times K + C + ER \times (CP-25)^{0.15}$$

K = 1 if exchange rate is between Rs25 and Rs65

ER/25 if ER is lower than Rs25

ER/65 if ER is higher than Rs65

C = Constant to be quoted by the bidder which shall not change through March 2012

ER = Exchange rate

CP = Crude price linked to avergar price of Dated Brent for FY2007 with a ceiling of US\$65/bbl and a floor of US\$25/bbl

### Scenario 1: Computation of selling price using a bidding constant (C) of 1

		Sensitivity of selling price of KG D6 gas to different levels of crude price and exchange rate (US\$/mn BTU)						
		Exchange rate (Rs/US\$)						
		55.0	50.0	45.0	40.0	35.0	30.0	25.0
Crude price (US\$/bbl)	25	2.06	2.27	2.52	2.84	3.24	3.78	4.54
	35	3.48	3.68	3.93	4.25	4.66	5.20	5.95
	45	3.63	3.84	4.09	4.40	4.81	5.35	6.11
	50	3.68	3.89	4.14	4.46	4.86	5.40	6.16
	55	3.73	3.94	4.19	4.50	4.91	5.45	6.21
	65	3.80	4.01	4.26	4.58	4.98	5.52	6.28
	75	3.80	4.01	4.26	4.58	4.98	5.52	6.28

### Scenario 2: Computation of selling price using a bidding constant (C) of 10

		Sensitivity of selling price of KG D6 gas to different levels of crude price and exchange rate (US\$/mn BTU)						
		Exchange rate (Rs/US\$)						
		55.0	50.0	45.0	40.0	35.0	30.0	25.0
Crude price (US\$/bbl)	25	2.23	2.45	2.72	3.06	3.50	4.08	4.90
	35	3.64	3.86	4.13	4.48	4.91	5.50	6.31
	45	3.79	4.02	4.29	4.63	5.07	5.65	6.47
	50	3.85	4.07	4.34	4.68	5.12	5.70	6.52
	55	3.89	4.12	4.39	4.73	5.17	5.75	6.57
	65	3.97	4.19	4.46	4.80	5.24	5.82	6.64
	75	3.97	4.19	4.46	4.80	5.24	5.82	6.64

Source: Infraline, Kotak Institutional Equities.

**Formula designed to keep pricing in a narrow band in rupee terms**

Selling price of gas from KG D-6 block at various levels of crude price and exchange rate (Rs/mn BTU)

**Scenario 1: Computation of selling price using a bidding constant (C) of 1**

		Sensitivity of selling price of KG D6 gas to different levels of crude price and exchange rate (Rs/mn BTU)						
		Exchange rate (Rs/US\$)						
		55.0	50.0	45.0	40.0	35.0	30.0	25.0
Crude price (US\$/bbl)	25	114	114	114	114	114	114	114
	35	191	184	177	170	163	156	149
	45	200	192	184	176	168	161	153
	50	203	195	186	178	170	162	154
	55	205	197	188	180	172	163	155
	65	209	200	192	183	174	166	157
	75	209	200	192	183	174	166	157

**Scenario 2: Computation of selling price using a bidding constant (C) of 10**

		Sensitivity of selling price of KG D6 gas to different levels of crude price and exchange rate (RS/mn BTU)						
		Exchange rate (Rs/US\$)						
		55.0	50.0	45.0	40.0	35.0	30.0	25.0
Crude price (US\$/bbl)	25	123	123	123	123	123	123	123
	35	200	193	186	179	172	165	158
	45	209	201	193	185	177	170	162
	50	212	204	195	187	179	171	163
	55	214	206	197	189	181	172	164
	65	218	209	201	192	183	175	166
	75	218	209	201	192	183	175	166

Source: Infraline, Kotak Institutional Equities.

## Economy

Sector coverage view

N/A

## India's 7.4% April 2007 infrastructure industries growth: Holding on

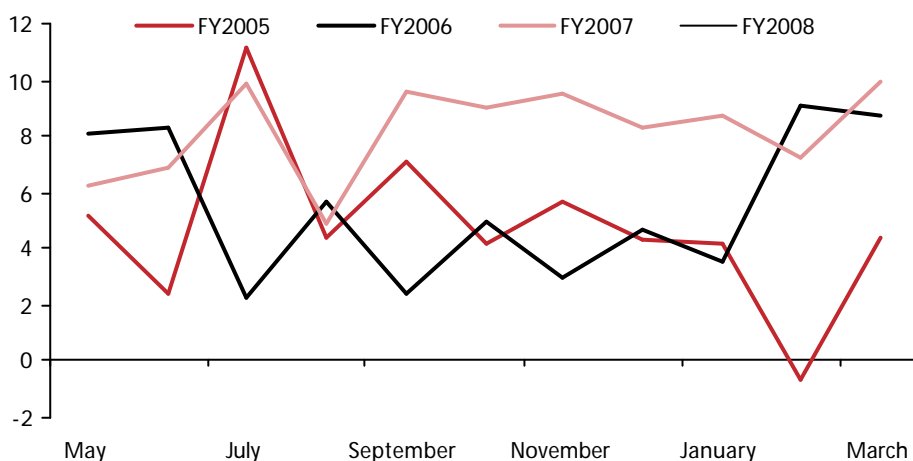
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- **Infrastructure up 7.4 % in April 2007 (7.3% last year)**
- **Electricity, steel up; crude up on Mumbai High effects**
- **Infrastructure industries approaching full capacity.**

Production of infrastructure industries worked out to 7.4% y-o-y in April 2007, comparable to 7.3% last year (Exhibits 1-2). This was led by a sustained increase in electricity generation and steel production. Crude oil production has also been higher because of the base effect of the August 2005 Mumbai High fire. Cement production decelerated to 5.1% from 12.2% in April 2006 on base effects. We continue to highlight that most infrastructure industries are now operating at close to capacity levels, reflecting the growing investment sensitivity of GDP. Refineries operated at 108.7% during April 2006 - February 2007 (99.4% last year). Steel producers worked at 96% capacity up from 92% last year. Capacity utilization in cement also climbed to 90% (86% in last year).

### Exhibit 1: Infrastructure industries continue to clock healthy growth

Production in infrastructure industries (y-o-y growth in %)



Source: Ministry of Industry, Government of India, with August 2005 revisions.

**Exhibit 2: Infrastructure industries**

Growth rate (%)

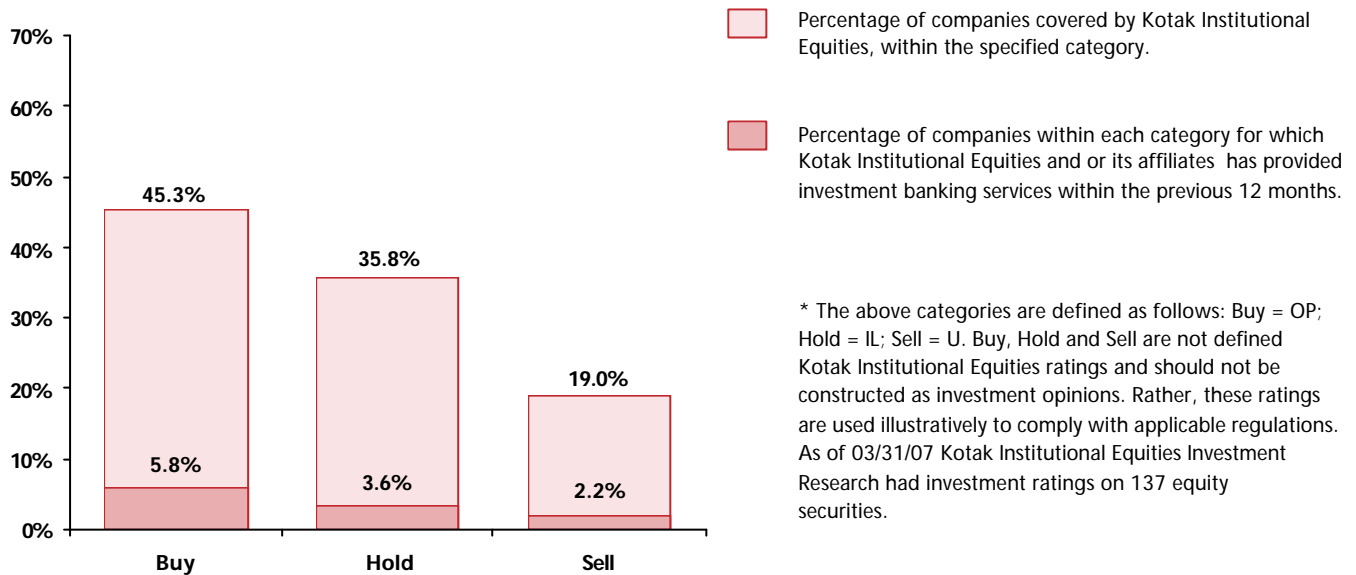
	Electricity	Coal	Finished Steel	Cement	Crude petroleum	Petroleum refinery products	Overall
Weight	10.2	3.2	5.1	2.0	4.2	2.0	26.7
High growth phase	6.2	5.3	11.3	10.1	1.8	4.9	6.9
Low growth phase	4.8	2.7	11.3	10.1	1.8	4.9	6.9
FY 2004	5.1	5.8	9.8	6.1	1.0	8.2	6.2
FY 2005	5.2	3.9	8.4	6.6	1.8	4.3	5.8
FY2006	5.1	6.6	11.2	12.4	(5.2)	2.1	6.2
<b>April 2006</b>	<b>5.9</b>	<b>3.4</b>	<b>10.1</b>	<b>12.2</b>	<b>(1.8)</b>	<b>13.1</b>	<b>7.3</b>
<b>April 2007</b>	<b>8.7</b>	<b>0.5</b>	<b>8.4</b>	<b>5.1</b>	<b>1.4</b>	<b>15.1</b>	<b>7.4</b>

Source: Ministry of Industry.

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Distribution of ratings/investment banking relationships



Source: Kotak Institutional Equities.

As of March 31, 2007

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#### Current rating system

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

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