

June 16, 2006

FOR PRIVATE CIRCULATION

**Equity**

	15 Jun 06	% Chg		
		1 Day	1 Mth	3 Mths
<b>Indian Indices</b>				
Sensex	9,545	6.9	(19.6)	(12.3)
Nifty	2,799	6.3	(20.6)	(13.3)
Banking	4,253	5.9	(21.5)	(20.0)
IT	2,207	7.6	(18.6)	(14.7)
Healthcare	2,967	4.9	(23.4)	(17.7)
FMCG	1,696	6.4	(22.8)	(16.7)
PSU	4,643	6.0	(24.0)	(20.4)
CNX Midcap	3,545	6.3	(28.4)	(23.7)
<b>World indices</b>				
Nasdaq	2,144	2.8	(3.8)	(6.8)
Nikkei	14,471	1.1	(7.9)	(7.5)
Hangseng	15,435	1.2	(3.7)	0.4

**Value traded (Rs cr)**

	15 Jun 06	% Chg - 1 Day
Cash BSE	2,935	0.3
Cash NSE	6,211	(9.1)
Derivatives	22,642.3	(1.3)

**Net inflows (Rs cr)**

	14 Jun 06	% Chg	MTD	YTD
FII	(363.4)	(344.3)	(6,565)	11,745
Mutual Fund	(338.3)	(15.7)	6,176	12,176

**FII open interest (Rs cr)**

	14 Jun 06	% Chg
FII Index Futures	9,315	8.8
FII Index Options	2,690	10.5
FII Stock Futures	8,646	8.5
FII Stock Options	102	5.5

**Advances/Declines (BSE)**

	15 Jun 06	A	B1	B2	Total	% Total
Advances	199	563	449	1211	72	
Declines	8	94	338	440	26	
Unchanged	0	5	25	30	2	

**Commodity**

	15 Jun 06	% Chg		
		1 Day	1 Mth	3 Mths
Crude (NYMEX) (US\$/BBL)	70.1	0.9	0.8	10.3
Gold (US\$/OZ)	577.1	3.1	(15.7)	4.8
Silver (US\$/OZ)	10.3	6.4	(26.9)	(3.7)

**Debt/forex market**

	15 Jun 06	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	7.76	7.75	7.52	7.40
Re/US\$	45.98	45.98	45.45	44.42

**Sensex**



Source: Bloomberg

**ECONOMY NEWS**

- The Sensex, taking a cue from the recovery in Asian and US markets, recorded a single-day gain of 616 points - the biggest in its history. FIIs were net buyers to the tune of approximately Rs 1.22 bn on Thursday. (ET)
- Service tax could be levied on interconnect user charges (IUC) paid by one telecom service provider to another. The revenue department is vetting a proposal to levy service tax on interconnect user charges (IUC) with retrospective effect. (ET)
- India and Japan are working on a comprehensive economic cooperation agreement, likely to be concluded by the end of the year. Commerce and industry minister Kamal Nath said bilateral trade between the two countries, which stood at \$5.5 bn, would double over the next three years. (BS)

**CORPORATE NEWS**

- The transaction between the **Birlas** and **Tatas** for the latter's 48% stake in Idea Cellular has been completed and the money (Rs 44.06 bn) deposited in an escrow account. This amount will be transferred to the Tata Group once the transaction is cleared by the DoT, industry sources said. (ET)
- **Ashok Leyland** is in talks with a global player for a tie-up to set up a light commercial vehicle (LCV) manufacturing plant in India. There has been considerable speculation in the market that a global player may pick up all or part of the stake currently held by **Fiat** in the company. (BL)
- **Nicholas Piramal India** is acquiring the Morpeth, UK manufacturing facility of **Pfizer**. According to an official release issued by Nicholas Piramal to the BSE on Thursday, this will expand the company's global footprint, particularly in the finished API, contained finished dosage, packaging and supply chain areas. (BS)
- **Infosys Technologies** said on Thursday that its upcoming campus at Mahindra City SEZ near Chennai would be the largest campus as it expects to hire some 25,000 people in three to four years. The company plans to invest Rs 12.5 bn over three to four years in expanding the facility. (BL)
- **Jubilant Organosys** seems to have identified the New Jersey-based life sciences company, **Cambrex**, as one of its potential acquisition targets, as it looks for big buys in the US and Europe. The company could unveil a bid with valuation topping \$500 mn following a due diligence in the next three to six months, said informed sources. (ET)
- **Bharti Airtel** is close to finalizing a contract with **Ericsson** for its 60 mn lines expansion plan, industry sources said. Bharti aims to add these lines over the next three years. Bharti had invited expressions of interest for GSM expansion in March this year. (ET)
- **Reliance Industries** plans to invite third party investments of up to Rs. 1,000 bn for developing the proposed 25,000-acre Haryana SEZ. The zone will be located off NH 8 in Gurgaon, bordering west Delhi, and moving northwards into Jhajjar district. (BS)
- A host of global players have approached **HDFC** for a tie-up in its non-life insurance venture. This follows differences between HDFC and its existing non-life insurance partner **Chubb**. (ET)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange

## FROM OUR RESEARCH TEAM

### MANAGEMENT MEET UPDATE

**Saurabh Gurnurkar**  
saurabh.gurnurkar@kotak.com  
+91 22 66341273

**Dipen Shah**  
dipen.shah@kotak.com  
+91 22 66341376

## MEGASOFT LTD (Rs.127, CY07 PE: 9x; BUY)

We recently spoke to the company on the latest developments within the company. We continue to remain positive on the longer-term prospects of Megasoft and maintain our positive bias on the stock.

We have been buoyant on Megasoft due to its model, which has been evolving towards a more profitable product business from a plain vanilla services business over the last eight quarters. The company's strong R&D backbone has developed the 'first of its kind' VOISE platform in addition to other telecom software products that make us positive on the company's prospects going forward.

### MAIN TAKEAWAYS

#### (a) VOISE's first client win in place, revenues expected to kick in from Q2CY06

Recently, the company announced its first win for VOISE, in the form of the US-based XERO Mobile, a new entrant into the US MVNO space. The company has also said that it is in talks with other mobile virtual network enablers (MVNEs)/MVNOs for its VOISE platform.

After our interaction with the management we expect revenues from this VOISE win to start kicking in from Q2CY06 and then scale up commensurately as and when Xero grows its own subscriber base. We expect this deal to garner revenues of close to \$9.5 mn over the next two years. We feel there could be potential upsides to our revenue projections from Xero based on their subscriber additions in the future.

Megasoft will be responsible for the management of an end-to-end network VOISE platform for enabling Xero's mobile launch that would also include the supply of several other professional services as the project moves forward. The XERO mobile network hopes to ramp up its nascent subscriber base to around 5 mn by 2007. (Source: company's website).

#### (b) Deal with Sonetel, a toehold in the VoIP space

Megasoft, in an initiative to tap the high growth segment of VoIP, has put in place a small team that will be developing a technology-based solution on the VoIP platform for Sonetel. This tie up with Sonetel is expected to bring in revenues of around \$1 mn over the next one year. We feel this move by the company is not significant in terms of revenue accrual but is favorable from a strategic perspective wherein the company is trying to establish a foothold in the fast growing VoIP domain.

#### (c) Rollout of IN billing solutions for clients on course

Within the telecom vertical, the company has been focusing on the network side (roaming products) as well as on the billing side (INfinet) of the business. These billing products are built on the company's proprietary WISE platform. We believe the company's rollouts for its billing solutions are progressing well in the African geography (Gamcel), Middle East and in India (Hutchison Essar). We believe these geographies enjoy strong growth rates in terms of mobile subscriber additions and Megasoft has a sizeable opportunity to scale up its revenues in line with the subscriber additions made by the service providers.

### (d) Expected acquisition; still in the pipeline

Our discussions with the management indicate the company is mulling the finalization of its proposed acquisition. The company has been looking at an acquisition for some time now. Through this acquisition, we believe the company will be looking to strengthen its sales and marketing (S&M) initiative. We believe that with the presence of clientele in the American geography it would serve the company well to boost its S&M team that could look at providing AMC for the clients in addition to leveraging the target company's referral value in the market.

## VALUATION AND RECOMMENDATION

Overall, we remain positive on the prospects of the company and think that a growing contribution from the telecom vertical on the back of a strong R&D setup will bode well for the company's profitability.

We maintain our earnings estimates for CY06 and CY07 where we expect the company to report an EPS of Rs. 10.8 per share and Rs. 14.3, respectively.

Based on our estimates, we arrive at a DCF-based fair value of Rs. 201 for the stock. At our target price of Rs. 201, the company would be trading at 14x our estimated CY07 earnings, a discount to our estimated fair value for larger peers from the products space. We maintain a **BUY** on Megasoft with a price target of Rs. 201, an upside of 58% from current price levels.

Future prospects					
Rs. mn	CY05	CY06E	% chg	CY07E	% chg
<b>Revenues</b>	<b>1,154</b>	<b>1,657</b>	<b>43.5</b>	<b>2,155</b>	<b>30.1</b>
Expenditure	883	1,235		1,579	
<b>EBDITA</b>	<b>271</b>	<b>422</b>	<b>55.5</b>	<b>576</b>	<b>36.7</b>
Depreciation	44.9	44.1		50.7	
<b>EBIT</b>	<b>226</b>	<b>378</b>	<b>66.9</b>	<b>526</b>	<b>39.2</b>
Interest	19.9	16.1		13.0	
Other Income	2.4	8.7		9.6	
<b>PBT</b>	<b>209</b>	<b>370</b>	<b>77.3</b>	<b>522</b>	<b>41.1</b>
Tax	7.6	20.7		57.5	
<b>PAT</b>	<b>201</b>	<b>350</b>		<b>465</b>	
Minority Int	0.1	1.2		3.1	
PAT after M I	201	348		462	
EO items	0.0	0.0		0.0	
PAT after EO items	201	348	73.2	462	32.6
<b>EPS (Rs)*</b>	<b>7.9</b>	<b>10.8</b>		<b>14.3</b>	
OPM (%)	23.5	25.5		26.8	
GPM (%)	19.6	22.8		24.4	
NPM (%)	17.4	21.0		21.4	

Source: Company; \*- For CY06 and CY07, fully diluted equity is Rs.324mn

- In our opinion, for a growing company like Megasoft it is vital to increase its marketing expenses to enhance visibility and acquire clientele. In our projections, we have assumed the PBIT margins for the telecom and life sciences verticals to dip over CY06 and CY07 factoring in an increase in the S&M expenses.
- However, with an increasing proportion of the high margin telecom business, overall margins (23.5% for CY05) are expected to improve going forward. These are expected to be around 25.5% in CY06 and 26.7% in CY07, respectively.
- We now expect the company to report revenues of Rs. 1.65 bn and profits of Rs. 348 mn, which would translate into an EPS of Rs. 10.8 for CY06. In CY07, we expect revenues to grow to Rs. 2.15 bn and profits to grow to Rs. 461 mn, translating into an EPS of Rs. 14.3.

## CONCERNS

### Retention of human capital

In a technology intensive business like Megasoft's, it is critical to retain key employees and attract new talent having sufficient domain knowledge.

The ability of the company's R&D function to keep ahead of the curve in terms of product development is directly related to the company's ability to retain key personnel.

### Fall in overall tariffs

Especially in case of ASP-based revenue models, revenues will depend on variations in tariffs, minutes of usage, etc for the mobile operator.

### Industry dynamics

An overall slowdown in the growth of the mobile market and/or the roaming segment globally will be a key concern for the space in which the company operates.

Rupee appreciation beyond our assumed levels of 43 per US dollar by FY08 end could provide a downward bias to our earnings estimates.

#### Summary table

Rs mn	CY03	CY04	CY05	CY06E	CY07E
<b>Sales</b>	<b>797</b>	<b>850</b>	<b>1,154</b>	<b>1,657</b>	<b>2155</b>
Growth (%)	99.8	6.5	35.9	43.5	30.1
<b>EBITDA</b>	<b>85</b>	<b>125</b>	<b>271</b>	<b>422</b>	<b>576</b>
EBITDA margin (%)	10.6	14.7	23.5	25.5	26.7
<b>Net profit</b>	<b>19</b>	<b>-60</b>	<b>201</b>	<b>348</b>	<b>462</b>
Net cash	225	184	63	-525	-855
<b>EPS (Rs)</b>	<b>0.8</b>	<b>-2.4</b>	<b>7.9</b>	<b>10.8</b>	<b>14.3</b>
Growth (%)	-256.9	-410.0	432.9	36.2	32.6
CEPS	2.1	-0.7	9.7	12.1	15.8
DPS (Rs)	0.0	0.0	0.0	3.0	4.0
RoE (%)	7.4	-22.9	39.8	33.6	29.2
RoCE (%)	9.4	15.1	26.6	28.7	31.0
EV/Sales (x)	4.3	4.0	2.9	2.2	1.5
EV/EBITDA (x)	40.8	27.4	12.1	8.5	5.6
P/E (x)	165.9	-53.5	16.1	11.8	8.9
P/Cash Earnings	59.3	-183.6	13.1	10.5	8.0
P/BV (x)	12.8	10.3	4.6	3.0	2.3

Source: Company, Kotak Securities Research

## Bulk deals

Trade details of bulk deals					
Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. Price (Rs)
15-Jun	Action Fin	Meena Mehta	B	100,000	0.50
15-Jun	Aftek Info	Goldman Sachs Investment	S	600,000	41.95
15-Jun	Alps Indust	V and U Caplease Pvt Ltd	B	82,131	77.75
15-Jun	Alps Indust	V and U Caplease Pvt Ltd	S	86,276	78.30
15-Jun	Federal Bank	Acacia Partners Lp	B	818,000	144.90
15-Jun	Gokaldas Exp	The Master Trust Bank	B	200,000	540.00
15-Jun	Gokaldas Exp	Prudential ICICI Trust	B	104,898	540.00
15-Jun	Gokaldas Exp	Reliance Capital Trustee	S	400,000	540.00
15-Jun	Granules Ind	Goldman Sachs Investment	B	60,000	84.84
15-Jun	Granules Ind	Equity Intelligence India	S	47,242	85.01
15-Jun	Hiran Orgoch	V and U Caplease Pvt Ltd	S	38,123	65.82
15-Jun	Intern Comb	Reliance Capital Asset	S	23,428	265.04
15-Jun	JJ Exporter	Lotus Capital Financial	B	47,000	58.00
15-Jun	JJ Exporter	Yogendra Kumar Gupta	S	47,100	58.00
15-Jun	Kanishk St.	Kamayani Engg. Products	S	200,000	25.99
15-Jun	Khaitan Elct	Micro Management	B	50,000	98.60
15-Jun	Khaitan Elct	Yogendra Kumar Gupta	S	50,000	98.60
15-Jun	Metalman Ind	Findeal Investments Priva	S	100,000	9.98
15-Jun	Moldtek Tech	Imperial Corporate Fin	B	50,000	40.39
15-Jun	Parekh Alum	ABN Amro Bank NV London B	S	29,500	97.94
15-Jun	PFLInfotech	Hemrajsinh S Veghela	S	38,100	8.52
15-Jun	Pioneer Inve	MahalaxmiInnovative	B	328,830	65.65
15-Jun	PRN Cap Mark	Forever Merchants	B	60,000	232.28
15-Jun	PRN Cap Mark	C M Share Services	S	60,000	232.28
15-Jun	Venus Remeds	Citigroup Global Markets	S	212,368	197.68
15-Jun	Worldw Le Ex	Samir Mukund Lal Shah	B	20,225	34.63
15-Jun	Worldw Le Ex	Samir Mukund Lal Shah	S	26,990	35.24
15-Jun	Yashraj Secr	P Renubala	B	25,000	35.45
15-Jun	Yashraj Secr	S Praveen Kumar	B	25,000	35.42
15-Jun	Yashraj Secr	Calcom Consultancy Service	S	9,096	34.60
15-Jun	Yashraj Secr	Shree Harivansha Securities	S	14,500	35.84

Source: BSE

## Forthcoming events

COMPANY/MARKET	
Date	Event
16-Jun	Exide Industries to consider stock split; Dredging Corporation of India to announce earnings & dividend
17-Jun	Financial Technologies (India) to announce earnings
19-Jun	Radico Khaitan to consider raising of funds
21-Jun	CESC Ltd to announce earnings and dividend
22-Jun	Amara Raja Batteries to announce earnings and dividend
26-Jun	VSNL, ONGC to announce earnings and dividend
27-Jun	Corporation Bank holds shareholders meeting; Reliance Industries holds annual shareholders meeting; Bata India to announce 2nd quarter earnings
30-Jun	State Bank of India holds shareholders meeting; Bharat Electronics to announce earnings and dividend

Source: Bloomberg

## Gainers & Losers

Nifty Gainers & Losers				
	Price (Rs)	% change	Index points	Volume (mn)
<b>Gainers</b>				
Infosys	2,727.1	9.7	14.3	1.2
ONGC	1,030.7	4.1	12.5	1.6
BHEL	1,835.8	14.4	12.1	0.7
<b>Losers</b>				
Oriental Bank	158.4	2.2	0.2	0.1
Reliance Energy	435.3	1.6	0.3	0.7
Tata Chemical	197.7	3.3	0.3	0.2

Source: Bloomberg

## Research Team

Name	Sector	Tel No	E-mail id
Jay Prakash Sinha	Economy, Banking, FMCG, Agro-Industry	+91 22 6634 1207	jay.sinha@kotak.com
Dipen Shah	IT, Media, Telecom	+91 22 6634 1376	dipen.shah@kotak.com
Sanjeev Zarbade	Capital Goods, Engineering	+91 22 6634 1258	sanjeev.zarbade@kotak.com
Teena Virmani	Construction, Mid Cap, Power	+91 22 6634 1237	teena.virmani@kotak.com
Awadhesh Garg	Pharmaceuticals	+91 22 6634 1406	awadhesh.garg@kotak.com
Apurva Doshi	Logistics, Textiles, Mid Cap	+91 22 6634 1366	doshi.apurva@kotak.com
Saurabh Gurnurkar	IT, Media, Telecom	+91 22 6634 1273	saurabh.gurnurkar@kotak.com
Vinay Goenka	Auto, Auto Ancillary, Sugar	+91 22 6634 1291	vinay.goenka@kotak.com
Shrikant Chouhan	Technical analyst	+91 22 6634 1439	shrikant.chouhan@kotak.com
Kaustav Ray	Editor	+91 22 6634 1223	kaustav.ray@kotak.com
K. Kathirvelu	Production	+91 22 6634 1557	k.kathirvelu@kotak.com

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